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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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QUESTIONS PRESENTED

The Maryland Insurance Code regulates the affairs of insolvent insurance companies and establishes a system in which priority is given to payment of policy beneficiary claims on a pro-rata basis. Inconsistently, 31 U.S.C. § 3713 provides that debts owed to the United States Government as a claimant by insolvent entities are to be paid ahead of all other debts. The McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, provides that the business of insurance shall be regulated by the states and that no act of Congress shall be construed to invalidate, impair or supersede any state law regulating the business of insurance.

The questions presented are:

1. Whether the McCarran-Ferguson Act requires that payment of policy beneficiary claims against an insolvent insurance company be governed by state insurance code provisions regulating the liquidation of an insolvent insurance company and requiring pro-rata payment of policy beneficiary claims against that company, including those of the United States Government, notwithstanding 31 U.S.C. § 3713, which purports to give the federal government a priority over similarly situated claimants?

2. Whether provisions of a state insurance code regulating the winding up of an insolvent insurance company's affairs and the payment of policyholder claims against that company is conduct of the "business of insurance" for purposes of the McCarran-Ferguson Act?

LIST OF PARTIES

The parties to the proceedings below were Petitioner, James A. Gordon, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland in Liquidation, and Respondents, United States Department of the Treasury and W.E. Douglas, Commissioner, United States Department of the Treasury, Fiscal Service.

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UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*,

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioner James A. Gordon, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland, respectfully prays that a writ of certiorari issue to review the opinion of the United States Court of Appeals for the Fourth Circuit, entered in the above-entitled proceeding on May 20, 1988.

OPINIONS BELOW

The decision of the United States Court of Appeals for the Fourth Circuit is reported at 846 F.2d 272 (4th Cir. 1988), and is reprinted in the appendix hereto, commencing at 1a.

The decision of the United States District Court for the District of Maryland is reported at 668 F. Supp. 483 (D. Md. 1987), and is reprinted in the appendix hereto, commencing at 6a.

JURISDICTION

Invoking federal jurisdiction under 28 U.S.C. §§ 1331(a), 2201-2202; and 5 U.S.C. § 701 *et seq.*, Petitioner brought this suit in the United States District Court for the District of Maryland. On August 31, 1987, the district court denied Petitioner's motion for summary judgment, and granted Respondents' motion for summary judgment. *See infra* at 22a.

Petitioner appealed, and on May 20, 1988, the United States Court of Appeals for the Fourth Circuit entered a judgment and opinion affirming the order of the district court. *See infra* at 5a. No petition for rehearing was sought.

The jurisdiction of this Court to review the judgment of the United States Court of Appeals for the Fourth Circuit is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES INVOLVED

1. 15 U.S.C. § 1011 *et seq.*, the McCarran-Ferguson Act (reprinted in full commencing at 23a).

2. 31 U.S.C. § 3713, Priority of Government Claims (reprinted in full commencing at 24a).

3. Md. Ann. Code art. 48A, § 132 *et seq.*, Rehabilitation and Liquidation (reprinted in full commencing at 25a).

4. Md. Ann. Code art. 48A, § 504 *et seq.*, Property and Casualty Insurance Guaranty Corporation (reprinted in full commencing at 53a).

STATEMENT OF THE CASE

A. The History Of Eastern Indemnity Company Of Maryland

Petitioner is a Special Deputy State Insurance Commissioner of Maryland ("the Special Deputy State Insurance Commissioner"), with powers derived directly from the Maryland Insurance Code. Md. Ann. Code art. 48A, §§ 133(5), 145. He holds this position by virtue of his appointment under Maryland law as the receiver for Eastern Indemnity Company of Maryland ("Eastern Indemnity"), an insurance company organized under the laws of Maryland and formerly doing business in more than 30 states.[1]

Although its chief line of business was issuing surety and fidelity bonds, Eastern Indemnity also wrote performance and payment bonds for construction projects, including "Miller Act" bonds for federal construction. *See* 40 U.S.C. § 270(a)-(e). Following an investigation launched in late 1984, the State of Maryland Insurance Division concluded that Eastern Indemnity's financial condition was dangerous to its policyholders and the public. Accordingly, the State initiated "delinquency proceedings" against the insurer pursuant to the Maryland Insurance Code. After a failed rehabilitation attempt, Eastern Indemnity was

[1] Because the liquidation of insurance companies is excluded from coverage under federal bankruptcy law, 11 U.S.C. § 109(b), the liquidation of insolvent insurance companies, as with other aspects of insurance regulation, has been an area of state, not federal, concern.

placed into liquidation and declared insolvent in 1985. *See* Md. Ann. Code art. 48A, §§ 141-142, 161.

B. The Maryland Statutory Regime Regulating Insurance Companies

Consistent with the exclusion of insurance company insolvency from the federal bankruptcy provisions of title 11 of the United States Code, Maryland law vests the Special Deputy State Insurance Commissioner, as the receiver for Eastern Indemnity, with specific powers to govern Eastern Indemnity's affairs. These powers include marshalling the company's assets, adjusting policyholder claims against the company, and making payments in accordance with the priority of payment system established by the Maryland Insurance Code. Md. Ann. Code art. 48A, § 132 *et seq.* Specifically, the Maryland Insurance Code provides that priority of payment from the assets of the Eastern Indemnity receivership is given to claims of policyholders, beneficiaries and insureds on a pro-rata, equal treatment basis ahead of all other claims, except for those representing employee compensation claims not in excess of $500.00, expenses of administering the receivership, and tax claims. Md. Ann. Code art. 48A, §§ 158, 158A.

As of October 1986, when the instant litigation was filed, Eastern Indemnity's liabilities exceeded $68 million while the receivership assets totaled only $1 million. Because the receivership's liquidated assets were insufficient to pay in full all claims within each priority class, the Maryland Insurance Code required the Special Deputy State Insurance Commissioner to make only pro-rata payments to claimants.

The potential loss to Eastern Indemnity policyholders is somewhat mitigated by the existence of the

Maryland Property & Casualty Insurance Guaranty Corporation ("the PCIGC"), also a creature of the Maryland Insurance Code. The PCIGC is responsible for paying a limited class of "covered claims" arising out of Eastern Indemnity policies written for Maryland residents. Md. Ann. Code art. 48A, § 504 *et seq.* Similarly, guaranty associations in some of the other states in which Eastern Indemnity did business may be responsible for payment of "covered claims" against Eastern Indemnity for insurance written for their residents.

Guaranty associations, including the PCIGC, provide only partial protection for policyholders, however. Some guaranty associations entirely exclude surety claims from their protection, while other associations impose ceilings on the maximum amount of a claim which will be paid. Significantly, the Maryland Insurance Code provides that the PCIGC and all other guaranty associations are subrogated to the claims of the policyholders they pay. Accordingly, the PCIGC and the other guaranty associations have a claim against the assets of the Eastern Indemnity receivership on an equal priority with other policyholder claims. Md. Ann. Code art. 48A, § 158A.

After subtracting all claims even potentially covered by guaranty fund payments from Eastern Indemnity's liabilities, there remains more than $18 million in policyholder, beneficiary and insured claims as well as the subrogation claims of the guaranty associations which must be satisfied exclusively from the $1 million assets of the Eastern Indemnity receivership.

C. The United States' Demand For Priority Of Payment, Contrary To The Payment Regime Established By The Maryland Insurance Code

On March 20, 1985, shortly after Eastern Indemnity was declared insolvent, Respondent, the Commissioner of the United States Department of the Treasury's Financial Management Service Office, asserted, on behalf of the United States and all of its "departments, agencies and instrumentalities and their contractors," a priority for payment of the federal government's claims against Eastern Indemnity, pursuant to 31 U.S.C. § 3713.[2] The federal government's claims against Eastern Indemnity arose principally from performance and payment bonds issued by Eastern Indemnity in which the United States and its agencies and instrumentalities were obligees.[3]

Accordingly, the priority demanded by the federal government was primarily for claims in which the government was a policyholder, beneficiary or insured of Eastern Indemnity, a position functionally identical to all other, albeit private sector, claimants. The government, however, demanded dollar-for-dollar payment of its claims under Section 3713, instead of the pro-rata payment which it would receive under the Maryland Insurance Code. Payment of the government's claims as demanded would consume all of the receivership assets, leaving nothing to pay either the

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[2] Section 3713, originally enacted in 1797, carries with it the threat of personal liability against the Special Deputy State Insurance Commissioner should he fail to comply with the priority demanded by the government.

[3] Although the Respondent did not attach a dollar value to the government's claims, the Special Deputy State Insurance Commissioner estimated these claims to be in excess of $3.9 million.

$18 million in policyholder claims not covered by guaranty funds, or the subrogation claims of the guaranty funds.

Respondents were informed that compliance with the government's requested priority would entirely consume Eastern Indemnity's liquid assets, result in wholesale denial of valid policyholder claims, and render nugatory the Maryland Insurance Code provisions regulating insurance company insolvencies and payment of claims. Respondents nevertheless continued to demand dollar-for-dollar payment under Section 3713, rejecting the requirement of the Maryland Insurance Code priority payment system that the federal government's policy beneficiary claims be paid on a pro-rata basis.

Accordingly, the Special Deputy State Insurance Commissioner filed suit pursuant to 28 U.S.C. §§ 1331(a) and 2201-2202, seeking a declaration that the payment of policyholder claims against Eastern Indemnity is governed by the provisions of the Maryland Insurance Code, as opposed to the federal priority statute. He took this position because the primary purpose of the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, is ensuring that the regulation of the business of insurance remain a matter of state - not federal - law and that state regulation be accomplished without federal interference.[4]

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[4] The relevant portion of the statute reads as follows:

> No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such

D. The Decisions Of The Courts Below

Noting that the facts were "basically undisputed," App. at 7a, the United States District Court for the District of Maryland decided the case on motions by each party for summary judgment. Although the trial court agreed that, if granted, the priority asserted by Respondents would invalidate, impair or supersede the applicable provisions of the Maryland Insurance Code, App. at 12a, the court rejected the argument that the Maryland provisions regulating payment of claims against insolvent insurance companies constitute the "business of insurance," a prerequisite for application of the McCarran-Ferguson Act preemption.[5] As support for its conclusion, the trial court relied upon the

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business. . . .

15 U.S.C § 1012(b).

[5] In support of his motion, the Special Deputy State Insurance Commissioner cited two district court cases to the contrary. Each directly holds that state insurance code provisions governing the liquidation of insolvent insurance companies constitute the regulation of the business of insurance under the McCarran-Ferguson Act. *Washburn v. Cochran*, 643 F. Supp. 554 (S.D. N.Y. 1986); *Idaho ex rel. Soward v. Internal Revenue Service*, 662 F. Supp. 60 (D. Idaho 1987), *app. pending*, No. 87-4057 (9th Cir.).

The district court found these precedents unpersuasive because they did not discuss and follow three decisions of this Court construing the McCarran-Ferguson Act in the context of that statute's narrow exemption of the business of insurance from the federal antitrust laws. *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982); *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979); and *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453 (1969).

test articulated by this Court in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982) for determining whether insurance company activity constitutes the business of insurance and is, therefore, exempt from the federal antitrust laws by virtue of the McCarran-Ferguson Act's narrowly construed antitrust exemption. App. at 14a.

Accordingly, the district court concluded that the McCarran-Ferguson Act was inapplicable and that the federal priority statute governed in lieu of the Maryland Insurance Code. Summary judgment was, therefore, entered in favor of Respondents.

The Special Deputy State Insurance Commissioner appealed to the United States Court of Appeals for the Fourth Circuit. That court declined to address the arguments of the Special Deputy State Insurance Commissioner and, in a brief *per curiam* opinion, merely adopted the opinion of the district court as its own. *See* App. at 5a.

REASONS FOR GRANTING THE WRIT

The decision below that state regulation of the winding up of an insolvent insurance company's affairs and the payment of policyholder claims made against it do not constitute regulation of the business of insurance for purposes of the McCarran-Ferguson Act raises several important unresolved questions.

I

The McCarran-Ferguson Act, the Primary Purpose of which is to Ensure Continued State Regulation of the Business of Insurance, Mandates that the Payment of Policyholder Claims Against an Insolvent Insurance Company be Governed by the Maryland Insurance Code

This case presents this Court with the significant and urgent task of deciding a conflict between two federal statutes which cannot coexist without action by this Court to clarify their meaning. Resolving that conflict will also permit harmonizing of two separate, superficially inconsistent lines of Supreme Court cases that have given ambiguous guidance to lower federal courts.

At stake is the stability of the multi-billion dollar insurance industry which, as the result of the McCarran-Ferguson Act, relies solely on state regulation. The immediate legal issue is whether payment of policyholder claims against an insolvent insurance company will be governed by the primary purpose of the McCarran-Ferguson Act, which is to ensure continued state regulation of the business of insurance, or instead by 31 U.S.C. § 3713, the sole purpose of which is to generate income for the federal government. By resolving this pressing question, this Court will also, for the first time in thirty years, be in a position to decide whether provisions of a state insurance code, designed to fulfill the paramount goal of insurance regulation, constitute the business of insurance for purposes of the McCarran-Ferguson Act. Numerous other states have similar insurance code provisions, the interpretation of which will be significantly affected by the outcome of this case.

As evidenced by the decision below, there exists a serious and unresolved conflict between two important federal statutes, each of which was adopted to further important, yet fundamentally different, national policies. On the one hand there is the McCarran-Ferguson Act, which itself is intended to accomplish two distinct goals: first, to ensure that the states will regulate the business of insurance, and second, to afford a limited antitrust exemption from federal antitrust laws to insurance companies. *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 218 n.18 (1979). On the other hand there is 31 U.S.C. § 3713, one of the first laws enacted by the republic, which was designed to raise revenue for the federal government. The holding below that Section 3713 governs instead of the McCarran-Ferguson Act results in the partial invalidation of the McCarran-Ferguson Act and the policies served by its primary goal. This Court has never before addressed this statutory conflict and, until it does, the ability of state insurance regulators to discharge their responsibilities to policyholders is in serious jeopardy.

There also exists serious uncertainty with respect to the definition of the term "business of insurance," as it is used in the McCarran-Ferguson Act. This uncertainty is caused by the decisions of this Court, which have not directly construed the primary purpose of the McCarran-Ferguson Act in thirty years. Instead, this Court's recent decisions construing the Act have been confined to the altogether different, secondary antitrust exemption purpose, without clarifying the limited nature of these decisions.[6] Conse-

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[6] As discussed more fully, *infra*, and as recognized by Justice

quently, lower federal courts are rendering decisions which call into question the continued validity of this Court's early decisions interpreting the McCarran-Ferguson Act and, therefore, lower federal courts are in need of prompt guidance from this Court in this important area.

It is well established that the primary purpose of the McCarran-Ferguson Act is to ensure continued state regulation of the business of insurance. *Royal Drug*, 440 U.S. at 218 n.18. Congress' goal in passing the statute was "*broadly* to give support to the existing and future state systems for regulating and taxing the business of insurance." *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 429 (1946) (emphasis supplied). The narrow antitrust exemption of the McCarran-Ferguson Act, from which the three-part *Pireno* test is derived, constitutes only a secondary purpose of the Act. *Royal Drug*, 440 U.S. at 218 n.18. Significantly, exemptions from the antitrust laws are to be narrowly construed. *Id.* at 231.

It is similarly well established that one of the broad goals of state insurance regulation is ensuring the solvency of insurance companies. *Securities and Exchange Commission v. Variable Annuity Life Ins. Co.*,

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Brennan in his dissenting opinion in *Royal Drug*, 440 U.S. at 233-38, this Court's early cases construing the McCarran-Ferguson Act concerned the statute's primary purpose of broadly ensuring that the states continued to regulate the business of insurance. *See, e.g., Federal Trade Commission v. National Casualty Co.*, 357 U.S. 560 (1958); *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408 (1946) and *Robertson v. California*, 328 U.S. 440 (1946). As will be demonstrated, these early McCarran-Ferguson Act cases are inconsistent with this Court's more recent pronouncements in the context of the Act's narrow antitrust exemption.

359 U.S. 65, 77 (1959) (Brennan, J., concurring). This Court has explicitly recognized that whether an insurance company will meet its contractual obligation and pay a covered claim when due is the "only concern" of the carrier's policyholder. *Pireno*, 458 U.S. at 132. Stated differently, the "reliability, interpretation and enforcement" of an insurance policy, i.e., whether an insurer will pay a covered claim, is at the heart of the relationship between the insurer and insured. *National Securities, Inc.*, 393 U.S. at 460.[7] Accordingly, the *Pireno* test, articulated in the antitrust context of the McCarran-Ferguson Act, is of dubious value in resolving a case such as this, which arises under the broad primary regulatory purpose section of the statute.

The Maryland Insurance Code provisions at issue directly regulate whether the covered claims of policyholders against insolvent insurers will be paid.

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[7] In *Royal Drug*, 440 U.S. at 223, this Court acknowledged that the Congress which enacted the McCarran-Ferguson Act was aware that the very purpose of insurance regulation was concern over insurer solvency. *See also* 91 Cong. Rec. 1481 (1945) (remarks of Sen. Ferguson); 90 Cong. Rec. 6564-65 (1944) (remarks of Rep. Vorys); and 90 Cong. Rec. 6526 (1944) (remarks of Mr. Hancock that "the solvency of the insurer is of prime importance. . ."). Additionally, learned insurance treatises support the proposition that unless a policyholder's claim is actually paid upon the occurrence of an insured risk, no risk has in fact been transferred. *See infra* at 22 n.13.

In this regard it is significant to recall that in *Royal Drug*, 440 U.S. at 210-12, this Court noted that because the phrase "business of insurance" is not defined in the McCarran-Ferguson Act, resort both to the legislative history of the statute and authoritative insurance treatises is necessary to discern the meaning of the phrase.

Through the statutory provisions cited, *supra*, the Maryland legislature has provided that covered policyholder claims against an insolvent insurer will be paid pro-rata in a certain priority, so as to fulfill the payment expectations of the maximum number of policyholders to as great an extent as possible.

Relying on *Pireno* and *Royal Drug*, the Fourth Circuit has nevertheless held that the Maryland Insurance Code provisions designed to fulfill the paramount goal of insurance regulation, protection of the policyholder, are preempted by a federal statute, which was designed to generate income for the United States and was passed at a time when modern insurance companies and regulatory programs did not exist. The effect of this ruling will result in the denial of millions of dollars in policyholder claims, and in this case wholly consume the assets available to the Special Deputy State Insurance Commissioner to administer the receivership in accordance with the goal of the Maryland Insurance Code: paying similarly situated claimants on a pro-rata basis. Accordingly, this Court should resolve the important questions presented concerning the interpretation of the McCarran-Ferguson Act's state regulatory provision and clarify the present uncertainty as to continued state regulation of insolvent insurance companies.

Simply put, *Pireno* and *Royal Drug* are inapplicable to the matters at bar because those cases involved efforts by insurance companies to use the McCarran-Ferguson Act as a shield from suits charging them with antitrust violations. As this Court pointed out in *Royal Drug*, the primary purpose of the McCarran-Ferguson Act was to "preserve state regulation of the activities of insurance companies." *Royal Drug*,

440 U.S. at 218 n.18. That purpose was manifestly not involved in *Royal Drug*, which concerned the McCarran-Ferguson Act's secondary purpose: affording insurance companies limited exemption from the federal antitrust laws. *Id.* at 207-10, 215, 217-18. Similarly, *Pireno* did not involve the primary regulatory purpose of the McCarran-Ferguson Act, but instead involved the Act's secondary antitrust function. *Pireno*, 458 U.S. at 126. The fundamental distinction between the Act's two purposes demonstrates the impropriety of invalidating a state statute regulating the payment of insurance claims, an issue arising under the statute's primary regulatory purpose, by employing the logic of two antitrust cases which arose under the Act's narrowly construed secondary purpose.

More importantly, application of the three-part *Pireno* test outside the context of the McCarran-Ferguson Act's secondary purpose antitrust exemption produces results directly conflicting with this Court's interpretations of the McCarran-Ferguson Act's primary regulatory purpose provision.[8] In *Robertson v. California*, 328 U.S. 440 (1946), decided the year after passage of the McCarran-Ferguson Act, this Court ruled that the California Insurance Code provisions requiring licensing of insurance companies and their brokers would constitute the regulation of the business of insurance under the McCarran-Ferguson Act. *Id.* at 462. That case involved the primary regulatory function of the McCarran-Ferguson Act, not its sec-

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[8] Under the three-part *Pireno* test, a practice constitutes the business of insurance if it: (a) involves the transfer or spreading of risk; (b) involves the relationship between insurer and insured; and (c) if all parties to the practice are within the insurance industry. *Pireno*, 458 U.S. at 127-29; App. at 3a.

ondary antitrust exemption purpose. The result reached upon application of the *Pireno* test to the facts of *Robertson*, however, directly conflicts with this Court's holding in *Robertson* because the practice under scrutiny in *Robertson* would not pass the first and most important prong of the three-part *Pireno* test: the requirement that insurance companies be licensed has nothing whatsoever to do with the underwriting or transfer of policyholder risk.

Similarly, in *Federal Trade Commission v. National Casualty Co.*, 357 U.S. 560 (1958), this Court held that state insurance code provisions governing insurance company advertisements constituted the regulation of the business of insurance under the McCarran-Ferguson Act, and that the Federal Trade Commission was, therefore, precluded from regulating this activity. Once again, the result reached if the *Pireno* test were to be applied to the facts of *National Casualty Co.* directly conflicts with this Court's ruling in *National Casualty Co.* The regulation of insurance company advertisement does not pass *any* prong of the *Pireno* test: it does not involve the underwriting or transfer of policyholder risk; it does not involve insurer-insured relationships; and it clearly encompasses third parties outside of the insurance industry.

This Court's decisions have produced a graphic conflict between the holdings in the primary regulatory purpose context in *Robertson* and *National Casualty Co.* and the decisions following the *Pireno* test. Under the *Pireno* analysis, *Robertson* and *National Casualty Co.* would have to be decided differently. This should not be so, however, because exemptions to the antitrust laws are to be narrowly construed, *Royal Drug*, 440 U.S. at 218 n.18, while the McCarran-Ferguson

Act's primary purpose of preserving state regulation of the business of insurance is to be broadly construed. *Benjamin*, 328 U.S. at 429. Thus, the rigorous *Pireno* test quite properly applies in cases arising under the McCarran-Ferguson Act's secondary purpose, exempting certain insurance company conduct from the federal antitrust laws, but not in cases such as the instant one which arise under the broadly construed primary purpose of the statute, ensuring continued state regulation of the business of insurance. Because this Court has not interpreted the Act's broadly construed state regulatory provision since long before it announced the *Pireno* test, clarification of the jurisprudence concerning the regulatory provisions of the McCarran-Ferguson Act is in order.[9]

The urgent need for clarification is illustrated by the conflict between the decision below and two recent United States District Court opinions. In *Idaho ex rel. Soward*, 662 F. Supp. 60, the court was faced with the identical issue presented in this case, i.e., whether the government has priority under Section 3713 over payments from the assets of an insurance receivership. In *Washburn*, 643 F. Supp. 554, the court was asked to decide whether provisions of a

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[9] In *Pilot Life Ins. Co. v. Dedeaux*, 107 S.Ct. 1549 (1987); *Metropolitan Life Ins. Co. v. Massachusetts*, 471 U.S. 724 (1985); and *Arizona Governing Committee v. Norris*, 463 U.S. 1073 (1983), this Court utilized the *Pireno* definition of the "business of insurance" as a guide in interpreting federal statutes other than the McCarran-Ferguson Act. Accordingly, those cases are inapplicable to the case at bar which directly involves construction of the primary state regulatory provision of the McCarran-Ferguson Act.

state insurance code dealing with the liquidation of an insolvent insurance company constituted the business of insurance for purposes of the McCarran-Ferguson Act. Unlike the courts below, these courts recognized that the purpose of the respective state insurance codes was to provide policyholders and the public with "cradle to grave" regulation of the insurance business, which includes regulation of the liquidation of an insolvent insurance company. Each court, therefore, concluded that the state liquidation provisions did constitute the business of insurance, and, in *Idaho ex rel. Soward*, that the priority sought by the United States Government under Section 3713 was precluded by the McCarran-Ferguson Act.

The conflict between this Court's holdings in *Robertson* and *National Casualty Co.* and the results reached in those cases when the *Pireno* test is applied, as well as the conflict between the decision below and the two district court decisions reaching the opposite result, demonstrates the need for this Court to clarify the status of the McCarran-Ferguson Act in the primary purpose state regulatory context.

II

The Issues Raised in This Petition are of Far-Reaching National Significance

The questions at issue are far reaching and of national significance. Most state insurance codes have provisions similar to that of Maryland, and give priority to payment of policyholder claims from the assets of an insolvent carrier ahead of other claims.[10] More-

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[10] *See, e.g.*, Colo. Rev. Stat. § 10-3-507 (1987 Repl. Vol); Conn.

over, the number of pending insurance company receiverships is large and growing. According to figures compiled by the National Association of Insurance Commissioners ("NAIC"), more than 100 insurance company receiverships were pending in 27 states as of 1986. *See* American Bar Association, *Reference Handbook on Insurance Company Insolvency* 621-41 (1986). The reality of insurance liquidations is that available assets are inevitably insufficient to pay all policyholder claims in full. *See, e.g.*, Traylor, "The Liquidation Process," in *Law and Practice of Insurance Company Insolvency* 62, 82, 86-87 (1986). In response to this reality, the various state insurance codes give priority of payment to policyholder claims so as to fulfill policyholder payment expectations to the maximum extent possible. The result reached by applying the test arising under the McCarran-Ferguson Act's narrowly drawn antitrust exemption frustrates this state regulatory program by permitting the federal government to step in front of policyholders to repay itself in full, and, as in this case, consume all of the assets which otherwise would have been available to pay policyholder claims.

Only action by this Court will eliminate this significant, recurring and growing problem. The legal issues and underlying policy issues are clear. Awaiting further, conflicting lower court decisions will unnecessarily create confusion in the insurance industry,

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Gen. Stat. § 38-462 (1982); Fla. Stat. § 631.271 (1987 Repl. Vol); Idaho Code § 41-3342 (1987 Cum. Supp.); Ill. Rev. Stat. ch. 73 § 205 (1988 Cum. Supp.); Mass. Gen. Laws Ann. ch. 175, § 180F (1988 Cum. Supp.); Ohio Rev. Code Ann. § 3903.42 (1987 Supp.); Pa. Stat. tit. 40, § 221.44; Tex. Ins. Code Ann. § 21.28B; Wis. Stat. §§ 645.68 (1)-(11) (1987 Cum. Supp.).

particularly in connection with the handling of insurance company insolvencies.

III

The Legislative History of the McCarran-Ferguson Act and Learned Insurance Treatises Demonstrate that the Relevant Maryland Insurance Code Provisions Regulate the Business of Insurance

Finally, the legislative history of the McCarran-Ferguson Act and learned insurance treatises demonstrate that the statutes in question manifestly regulate the business of insurance. This is true even assuming, *arguendo*, that the *Pireno* test is relevant in ascertaining whether the Maryland Insurance Code provisions dealing with the liquidation of insolvent insurance companies regulate the business of insurance.

In this regard, it is significant to note that in discharging his statutory obligation of paying covered claims made against Eastern Indemnity, the Special Deputy State Insurance Commissioner must, as a preliminary matter, determine whether a purported policyholder claim is, in fact, covered by the policyholder's Eastern Indemnity policy. In doing so, he acts as the adjustor for the insurance company. Md. Ann. Code art. 48A, § 132. In *Pireno*, 458 U.S. 134 n.8, this Court explicitly recognized that claims adjustment does, indeed, constitute the business of insurance. Accordingly, even under *Pireno*, it is clear that the regulations at issue here, which empower the Special Deputy State Insurance Commissioner to ad-

just claims against Eastern Indemnity, regulate the business of insurance.[11]

With regard to the first element of the *Pireno* test, whether the statutes in question relate to the underwriting and transfer of policyholder risk, it is important to recall that the phrase "business of insurance" is not defined in the McCarran-Ferguson Act. Accordingly, in *Royal Drug*, 440 U.S. at 210-12, this Court instructed that resort to both the legislative history of the Act and authoritative treatises on insurance are necessary to discern the meaning of this phrase. Significant portions of the legislative history of the McCarran-Ferguson Act demonstrate clear Congressional awareness that insurance is a unique commodity, because it involves the payment of a premium for protection which might not be needed for years to come. If insurance is to fulfill the promise of protection purchased by the policyholder, the company selling the insurance must be able to back up its promise with actual payment at the time of loss.[12]

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[11] The dissenting opinion in *Royal Drug*, 440 U.S. at 236-237, recognized that what the states considered to be regulated as insurance at the time the McCarran-Ferguson Act was passed is relevant in defining the contours of "the business of insurance." Moreover, the dissent also recognized the importance of this Court's earlier decisions construing the Act's primary purpose state regulatory provision. *Royal Drug*, 440 U.S. at 235-237.

[12] *See* remarks of Senator Ferguson, one of the authors of the McCarran-Ferguson Act, as to the purposes of the statute:

> The sale of insurance is not the same as the sale of an article in a store. When one buys an article in a store, he brings it home with him. In the case of insurance, he buys a promise to pay upon the hap-

The same concept, that the essence of insurance is the fulfillment of the transfer of risk by the actual payment of benefits upon the occurrence of a loss, is well supported by learned commentators on the insurance industry.[13]

The regulatory procedures of the Maryland Insurance Code governing insurance company liquidation, like those in virtually every other state, are aimed at fulfilling the promise of insurance by seeing to it that claims of policyholders, insureds and beneficiaries receive priority payment in the event of insurer insolvency. Indeed, the insolvency provisions of the Maryland Insurance Code are but a single part of a regulatory whole which applies to all aspects of insurance from cradle to grave. The holding below arose from the courts' failure to appreciate that this Court's opinions in *Royal Drug* and *Pireno* did not address direct efforts by state insurance regulators to enforce provisions of their insurance codes for the protection of the public. Rather, *Royal Drug* and *Pireno* involved efforts by insurance companies to invoke the Mc-

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> pening of a certain event, and that event may be the burning of his home. If the company is not sound and solvent at the time the house burns, or at the time the claim is made, there is not insurance at all. That is what we have tried to avoid.

91 Cong. Rec. 1481 (1945). *See also* 90 Cong. Rec. 6564-65 (1944) (remarks of Rep. Vorys); 90 Cong. Rec. 6526 (1944) (remarks of Rep. Hancock).

[13] *See* 2 G. Richards, *The Law of Insurance*, § 207 (W. Freedman, 5th ed. 1952); *Couch on Insurance* § 1:3 (2d rev. ed. 1984); William and Heins, *Risk Management and Insurance* 279 (5th ed. 1985); Athearn and Pritchett, *Risk and Insurance* (5th ed. 1984).

Carran-Ferguson Act as protection against enforcement of federal antitrust laws and this Court made clear in *Royal Drug* that the antitrust exemption at issue was to be narrowly construed. Only action by this Court can clear up the confusion surrounding interpretation of the McCarran-Ferguson Act's primary regulatory context.

Similarly, the Maryland Insurance Code liquidation provisions pertain to the relationship between the insurer and the insured and, therefore, constitute the regulation of the business of insurance. In *National Securities, Inc.*, 393 U.S. at 460, this Court ruled that the very heart of the business of insurance was the "relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation and enforcement—these were the core of the business of insurance." The Maryland Insurance Code's liquidation provisions are designed to assure the reliability and enforcement of insurance policies, even after insolvency of the company which issued them, by mandating priority payment to the policyholders.[14]

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[14] Finally, the Maryland Insurance Code provisions at issue involve only insurance industry parties. The Special Deputy State Insurance Commissioner, as receiver for Eastern Indemnity, serves as the adjustor of claims against Eastern Indemnity. Md. Ann. Code art. 48A, § 132. In this capacity, he determines whether a purported policyholder claim is, in fact, covered by the particular Eastern Indemnity policy in question. Only if the Special Deputy State Insurance Commissioner resolves that question in favor of the policyholder and determines that the claim is covered by the Eastern Indemnity policy does the policyholder even have a right to claim against the assets of the receivership in the priority established by the Maryland Insurance Code.

Until this Court acts to clear up the confusion surrounding state efforts to protect policyholders in the event of insurance company insolvency, insurance regulatory efforts to protect policyholders in Maryland and virtually every other state will be threatened. Given the large number of pending insurance company liquidations, and the certainty of more in the future, the issues presented in this case are of widespread importance and merit prompt resolution by this Court.

CONCLUSION

For all of the foregoing reasons, the petition for certiorari should be granted. If Petitioner is correct and the Maryland statutes regulate the business of insurance, then the case should be remanded to the district court for entry of summary judgment in Petitioner's favor so that Eastern Indemnity's policyholders may all be paid on a pro-rata basis, rather than permitting the federal government to seize all of Eastern Indemnity's available assets under a statute designed to assist the government in its collection efforts.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 87-1703

JAMES A. GORDON, Special Deputy State Insurance Commission of Maryland and Receiver, Eastern Indemnity Company of Maryland in Receivership

Plaintiff-Appellant

versus

UNITED STATES DEPARTMENT OF THE TREASURY; W.E. DOUGLAS, Commissioner, United States Department of the Treasury, Fiscal Service;

Defendants-Appellees

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS; ILLINOIS INSURANCE GUARANTY FUND; PROPERTY AND CASUALTY INSURANCE GUARANTY CORPORATION; WISCONSIN INSURANCE SECURITY FUND; TEXAS PROPERTY AND CASUALTY INSURANCE GUARANTEE ASSOCIATION; JAMES T. ODIORNE, in his capacity as Texas Ancillary Receiver for Eastern Indemnity Company

Amici Curiae

Appeal from United States District Court for the District of Maryland, at Baltimore. Walter E. Black, Jr., District Judge. (CA-86-3354-B)

Argued: May 4, 1988 **Decided: May 20, 1988**

Before WINTER, Chief Judge, SPROUSE, Circuit Judge, and KAUFMAN, Senior United States District Judge for the District of Maryland, sitting by designation.

Paul W. Grimm (David D. Gilliss, JORDAN, COYNE, SAVITS & LOPATA on brief) for Appellant. (Carole J. Olson, NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS on brief) for Amicus Curiae National Association of Insurance Commissioners (Thomas W. Jenkins, Hugh C. Griffin, Mark R. Goodman, LORD, BISSELL & BROOK on brief) for Amici Curiae The Illinois Insurance Guaranty Fund, The Property and Casualty Insurance Guaranty Corporation, The Texas Property and Casualty Insurance Guarantee Association, The Wisconsin Insurance Security Fund, and James T. Odiorne in his capacity as Texas Ancillary Receiver for Eastern Indemnity Company of Maryland. Sandra P. Spooner, Deputy Director (Richard K. Willard, Assistant Attorney General; J. Christopher Kohn, Director, Civil Division, DEPARTMENT OF JUSTICE on brief) for Appellees.

PER CURIAM:

James A. Gordon appeals the district court's judgment that the United States, in its capacity as a policyholder, is entitled to priority of payment in the liquidation of an insolvent insurance company, Eastern Indemnity Insurance Company (EICOM). *See* Gordon v. United States Department of the Treasury, 668 F. Supp. 483 (D. Md. 1987). As Special Deputy State Insurance Commissioner of Maryland and Receiver for EICOM, Gordon contends that Maryland state law governing the priority of payment of such claims, Md. Ins. Code Ann. art. 48A, §§ 158, 158A (1986), constitutes state regulation of the "business of insurance" within the meaning of the McCarran-Ferguson Act of 1945, 59 Stat. 33, as amended, 15 U.S.C. §§ 1011-15 (1982), and should therefore preempt, by operation of 15 U.S.C. § 1012(b), the government's claim to priority under 31 U.S.C. § 3713 (1982).

The district court concluded that the liquidation of an insolvent insurance company and the determination of the priority of payment of claims against the insolvent do not constitute the "business of insurance" within the meaning of the McCarran-Ferguson Act. It therefore held that the government's claim under the federal priority statute could prevail over a contrary state regulation of the business of insurance companies without contravening 15 U.S.C. § 1012(b). Its decision was properly guided by the Supreme Court decisions in Group Life & Health Insurance Co. v. Royal Drug Co., 440 U.S. 205 (1979), and Union Labor Life Insurance Co. v. Pireno, 458 U.S. 119 (1982), construing the term "business of insurance."[1]

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[1] In *Pireno*, the Supreme Court set forth three factors relevant to whether a practice is part of the "business of insurance": whether the practice has the effect of transferring or spreading a policyholder's risk; whether the practice is an integral part of the policy relationship between the insurer and the insured; and whether the practice is limited to entities within the insurance industry. *Pireno*, 458 U.S. at 129.

We reject Gordon's contention that the district court erred in relying on these opinions outside of the antitrust context. The Supreme Court's discussions of the definition of "business of insurance" in *Pireno* and *Royal Drug* are not, expressly or by logical implication, limited to the antitrust context. *See, e.g.,* Pilot Life Insurance Company v. Dedeaux, ___ U.S. ___, 107 S. Ct. 1549, 1553-54, 95 L.Ed.2d 39, 48-50 (1987) (whether Mississippi law of bad faith is state law regulating insurance); Metropolitan Life Insurance Co. v. Massachusetts, 471 U.S. 724, 743 (1985) (applying similar preemption language to state mandated-benefits law).

We agree with the district court's application of *Pireno*'s first factor: for the reasons given by the district court, the risk of insurer insolvency is certainly qualitatively distinct from the risk the policyholder seeks to transfer in an insurance contract. *See* 668 F. Supp. at 489-90. In some contexts such as an insurer's liquidation, *Pireno*'s first factor (whether a practice has the effect of transferring or spreading the policyholder's risk) may justifiably play a preeminent role in the § 1012(b) analysis. However, it is not necessary to review the correctness of the district court's statement that the first of the *Pireno* considerations should be a categorically "indispensable" requirement for a finding that a practice constitutes the "business of insurance." *See* 668 F. Supp. at 490-91. The district court's characterization of this factor as indispensable was not necessary to reach the result it did; the court did discuss the other two factors elaborated in *Pireno,* correctly concluding that they also weighed in favor of its holding that Maryland's regulation of the liquidation process of insurance companies, while perhaps the regulation of the business of insurers, was not the regulation of the "business of insurance" within the meaning of McCarran-Ferguson. *Id.* at 491; *see Royal Drug,* 440 U.S. at 211.[2]

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[2] *But see* Idaho ex rel. Soward v. United States, 662 F. Supp. 60

We decline to decide whether the first factor of *Pireno* may in some instances or in all cases be an indispensable requirement for a finding that a certain practice constitutes the "business of insurance." In all other respects, we are satisfied with what the district court said, and we adopt as our opinion that of the district court, 668 F. Supp. 483 (D. Md. 1987).

AFFIRMED.

(D. Idaho) (failing to discuss *Pireno* or *Royal Drug*), *appeal pending*, No. 87-4057 (9 Cir. 1987); Washburn v. Corcoran, 643 F. Supp. 554 (S.D.N.Y. 1986) (same).

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

JAMES A. GORDON, SPECIAL DEPUTY STATE INSURANCE COMMISSIONER OF MARYLAND AND RECEIVER, EASTERN INDEMNITY COMPANY OF MARYLAND IN RECEIVERSHIP	*	CIVIL NO. B-86-3354
v.	*	
UNITED STATES DEPARTMENT OF THE TREASURY, W. E. DOUGLAS, COMMISSIONER, UNITED STATES DEPARTMENT OF THE TREASURY, FISCAL SERVICE	*	

Filed: August 31, 1987

Paul W. Grimm, Esq., and David D. Gilliss, Esq., of Baltimore, Maryland, for Plaintiff.

Robert N. McDonald, Esq., Assistant United States Attorney, of Baltimore, Maryland, and J. Christopher Kohn, Esq., and Sandra P. Spooner, Esq., of Washington, D.C. for Defendants.

BLACK, DISTRICT JUDGE.

This case presents for resolution the always problematic situation that arises when a company lapses into insolvency and there is simply not enough money to satisfy each of the outstretched hands. The complexity of this insolvency is compounded by the existence of private as well as gov-

ernment creditors and a conflict in state and federal priority statutes. Whether the general rule of governmental priority shall apply to the facts of this particular case hinges exclusively upon the issue of whether the process of liquidating an insolvent insurance company and paying claimants constitutes the "business of insurance."

The facts underlying this case are basically undisputed. The Eastern Indemnity Insurance Company (hereinafter "EICOM") was licensed by the State of Maryland to do business in 1980. Its insurance business rapidly expanded to include more than thirty states throughout the United States. Primarily, its business involved the underwriting of surety bonds for contractors.

In 1984, the State Insurance Commissioner launched an investigation into the financial affairs of EICOM, and EICOM was thereafter placed into voluntary rehabilitation as provided by the Maryland Insurance Code. Md. Ann. Code art. 48A, § 132 (1957). In 1985, the Circuit Court for Montgomery County, Maryland, ordered the liquidation of EICOM, and the company was then declared to be insolvent. The plaintiff, James Gordon, acting in his capacity as Special Deputy State Insurance Commissioner of Maryland, was appointed Receiver for EICOM. Gordon was to handle the day-to-day activities involved in the liquidation of this failed insurance business.

Among the duties of Gordon as Receiver was the settlement and supervision of the claims of the policyholders of EICOM. In accordance with the Maryland Insurance Code, a date was established by which time the claimants of EICOM were to file their claims or be forever barred. After the passage of the deadline, Gordon determined that the claims filed exceeded 75 million dollars. Though the amount of their assets is not easily calculable, it is, in any event, far less than the amount necessary to satisfy the claimants in full. Of the more than 75 million dollars in claims filed against EICOM, approximately 61 million dol-

lars are made up of claims submitted by principals, obligees, material suppliers and subcontractors in connection with surety bonds issued by EICOM. Many of the projects for which EICOM issued performance and payment bonds were Miller Act construction projects. Thus, the United States Government is a claimant in addition to a number of private contractors.

By letter to Gordon from the defendant, W.E. Douglas, on behalf of the defendant, the U.S. Department of Treasury, the government asserted priority status to the assets of EICOM, which are subject to the control and administration of the plaintiff Gordon, in his official capacity as receiver for EICOM. The defendants also advised Gordon that, under the federal priority statute, he could be held personally liable for distributing assets in contravention of the statute. This litigation followed. On October 31, 1986, the plaintiff filed a complaint in federal court alleging that the action by the defendants in asserting a priority is illegal because it invalidates, impairs or supersedes provisions of the Maryland Insurance Code enacted for the purpose of regulating the business of insurance in contravention of the McCarran-Ferguson Act.[1] The plaintiff has sought a declaratory judgment that the defendants' assertion of a priority is illegal because it violates the McCarran-Ferguson Act and, further, that the defendants not take action to enforce the personal liability provision of the federal priority statute against Gordon.

This case involves the interplay of three statutes—two federal statutes and the Maryland Insurance code. Broad policy statements underlie each of their statutory schemes. The first, section 3713 of Title 31 of the United States

[1] The complaint also alleged that the claims of materialmen, suppliers and subcontractors pursuant to Miller Act construction projects "do not constitute debts owed to the United States"; however, the parties have resolved this issue without court intervention and, therefore, it need not be addressed here.

Code, establishes an absolute priority of government claims when an individual is insolvent and makes a voluntary assignment of property, has its property attached, or commits an act of bankruptcy.[2] It was Congress' purpose in enacting § 3713 to "protect the interest of the government in collecting money due to it where property of an insolvent debtor is involved." *W.T. Jones and Company v. Foodco Realty, Inc.*, 318 F.2d 881, 885 (4th Cir. 1963). Its provisions have been in effect since 1797, without any significant modifications. *U.S. v. Emory*, 314 U.S. 423, 428 (1942). Section 3713 is the government's authority for asserting a priority over the assets of EICOM. Moreover, subsection (b) expressly provides that Gordon, as representative of EICOM, is personally liable to the government for paying debts ahead of the governmental priority.[3]

The Maryland Insurance code establishes a comprehensive scheme for administering the liquidation of insolvent insurance companies. An important part of this Code is devoted to defining the types of claims which may be filed against an insurance company undergoing liquidation, and

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[2] Section 3713 provides in pertinent part that,

> (a)(1) A claim of the United States Government shall be paid first when—
>
> (A) a person indebted to the Government is insolvent and—
>
> (i) the debtor without enough property to pay all debts makes a voluntary assignment of property;
>
> (ii) property of the debtor, if absent, is attached; or
>
> (iii) an act of bankruptcy is committed . . . .

31 U.S.C. § 3713 (1983).

[3] "A representative of a person or an estate (except a trustee acting under Title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government." 31 U.S.C. § 3713(b) (1983).

creating priorities for payment of these claims. For example, wages to officers and employees are paid first, administrative expenses are paid next and tax claims occupy the third priority. *See,* respectively, Md. Ann. Code art. 48A §§ 158 and 158A (1986). The category of priority claims relevant to this litigation is the fourth priority, namely, "[c]laims by policyholders, beneficiaries, and insureds . . . ." This category represents by far the largest amount of claims. The plaintiff contends that the claims of the government are on the same priority level as all "policyholders, beneficiaries, and insureds" and, therefore, fall within the fourth priority. The government disagrees and cites 31 U.S.C. § 3713. Indeed, if it were not for the special nature of this case, implicating the insurance industry, the outcome of this dispute would be clear: the claims of the government would take priority by virtue of § 3713.

The McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015, was enacted in 1945 due to congressional concern over federal regulation of insurance, traditionally a function of the states:

> Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest . . . .

15 U.S.C. § 1011 (1976); *see* S.Rep. No. 20, 79th Cong., 1st Sess., 2 (1945); H.R. Rep. No. 143, 79th Cong., 1st Sess., 2-3 (1945), U.S. Code Cong. Serv. 1945, p. 670 and the discussion of the Supreme Court's decision in *United States v. South-Eastern Underwriters Assn.,* 322 U.S. 533 (1944). Congress' second concern was the relationship between insurance ratemaking and the antitrust laws "[b]ecause of the widespread view that it is very difficult to underwrite risks in an informed and responsible way without intraindustry cooperation." *Group Life & Health Insurance v. Royal Drug Co.,* 440 U.S. 205, 221 (1979).

Consequently, a partial exemption from the antitrust laws was included in the McCarran-Ferguson Act. 15 U.S.C. § 1012(b)(1976). The critical passage in the McCarran-Ferguson Act is that,

> [n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance . . . .

Id. Thus, the phrase "business of insurance" was born, and, so long as a state acts to regulate the "business of insurance," its legislation is free of the intervention of Congress, at least in the absence of a specific law enacted by Congress as to a given matter. *See* 19 *Appleman, Insurance Law and Practice* § 10323 (1982). Federal laws will not be construed to supersede state laws regulating the "business of insurance."

The sole question before this Court is whether the State of Maryland was acting to regulate the "business of insurance" when it established the statutory scheme regarding the liquidation of insolvent insurance companies and the priorities of claimants or policyholders for payment.[4] This narrow issue was fully briefed by the parties and the Court heard oral argument of counsel. Amicus curiae briefs were filed on behalf of the National Association of Insurance Commissioners and on behalf of the Illinois Insurance Guaranty Fund, the Property and Casualty Insurance Guaranty Corporation, and the Wisconsin Insurance Security Fund. The matter is formally before this Court on Cross-Motions for Summary Judgment. The Court notes at the outset that summary judgment is clearly appropriate where the Court is faced with a motion and

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[4] The question of whether other portions of the Maryland Insurance Code regulate the "business of insurance" is not before the Court and is not relevant to the Court's opinion and rulings in this case.

countermotion for summary judgment, wherein all parties admit to undisputed facts and are merely seeking a declaration of the law.

In broad terms, the legal question presented to the Court is whether the strictures of the McCarran-Ferguson Act afford protection to the state of Maryland's priority scheme for claimants of insolvent insurance companies. In order for the McCarran-Ferguson Act to apply, three elements must be met: (1) there must be a state statute intended to regulate or tax, (2) the "business of insurance" (3) which is invalidated, impaired, or superseded by an Act of Congress not expressly related to the business of insurance. Clearly, the Maryland Insurance Code was intended to regulate the insurance industry. Reorganization of insolvent insurance companies is a matter of state law and is handled through insolvency proceedings in state court. *Universal Marine Insurance Company, Ltd. v. Beacon Insurance Company,* 768 F.2d 84, 88 (4th Cir. 1985). Equally clear is that the federal priority statute "invalidates, impairs or supersedes" the priority scheme set forth in the state statute. Thus, the focus in this case is solely on the "business of insurance" issue.

Through several recent opinions, the Supreme Court has enunciated the considerations to use in deliberating on whether action by the state constitutes regulation of the "business of insurance" such that a federal law cannot operate to "invalidate, impair or supersede" its provisions. These Supreme Court cases effectively define and limit the antitrust exemption set out in the McCarran-Ferguson Act and are the controlling standards in determining what constitutes the "business of insurance." *See also, State of Maryland v. Blue Cross and Blue Shield,* 620 F. Supp. 907, 913 (D. Md. 1985).

Helpful to the Court's understanding of what constitutes the "business of insurance" is Justice Stewart's simple instruction in *Royal Drug,* 440 U.S. at 211, that the "busi-

ness of insurance companies."[5] In *Royal Drug,* a group of nonparticipating pharmacists brought an antitrust action against an insurance company claiming that they had entered into agreements with participating pharmacists to fix the retail price of drugs. Guided by congressional intent to establish only a limited exemption to the antitrust laws, the Court examined the allegedly illegal pharmacy agreements in light of the general concept of "insurance." The Court recognized two important features. First, that the primary element of insurance is the "spreading and underwriting of a policy-holder's risk." *Royal Drug,* 440 U.S. at 211. Thus, the concept of insurance involves some risk-taking on the part of the insurance company. The Court found that the pharmacy agreements with the insurance company in order to minimize its costs were unconnected to the basic contractual obligation the insurance company had made with its insureds to cover the cost of their prescription drugs.

The second common aspect of insurance is the existence of a contract between the insurer and the insured. *Id.* at 215. Citing the Court's earlier language in *Securities and Exchange Comm. v. National Securities, Inc.,* 393 U.S. 453, 460 (1969), Justice Stewart wrote,

> The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement—these were the core of the 'business of insurance.' Undoubtedly, other activities of insurance companies relate so closely to their status as reliable insurers

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[5] *See also,* Justice Marshall's observation in *Securities and Exchange Comm. v. National Securities, Inc.,* 393 U.S. 458, 459 (1969) regarding the history of the McCarran-Ferguson Act: "The statute did not purport to make the States supreme in regulating all the activities of insurance *companies;* its language refers not to the persons or companies who are subject to state regulation, but to laws 'regulating the *business* of insurance.' "

> that they to [sic] must be placed in the same class. But whatever the exact scope of the statutory term, it is clear where the focus was—it was on the relationship between the insurance company and the policyholder.

Royal Drug, 440 U.S. at 215-16. The Court concluded that the pharmacy agreements were in no way related to the contractual relationship between the insureds and the insurance company. The fact that the pharmacy agreements were entered into in order to lower the cost of premiums or affect their status as a reliable insurer was reflective of many of the business decisions made by an insurance company. To interpret otherwise, the Court wrote, would be to extend the definition of "business of insurance" to almost every business decision of an insurance company. *Id.* at 217. The conclusion of the Supreme Court in *Royal Drug* was that the insurance company was not exempt from the antitrust laws because the pharmacy provider agreements were not regulation of the "business of insurance." After *Royal Drug*, it was clear that, though many aspects of insurance companies are regulated by state law, they do not necessarily constitute the "business of insurance." Provider agreements by insurance companies for the purchase of goods and services from third parties at a set price were not the "business of insurance."[6]

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[6] In *Royal Drug*, the Supreme Court discussed also the concept of "advance-payment medical-benefits plans" as distinguished from insurance. At the time of the enactment of the McCarran-Ferguson Act, corporations organized for the purpose of providing their members with medical services and hospitalization were not considered to be engaged in the insurance business at all, and thus were not subject to state insurance laws. *Id.* at 225-26. The Court went on to find that, even if these plans were considered to be insurance by various state legislatures, the incorporation of provider agreements to lower cost of prescription drugs would still not be considered the "business of insurance." The provider agreements were analogized to many statutes regulating diverse aspects of these advance payment plans (or of insurance plans)

The Supreme Court addressed the concept of "business of insurance," and narrowed its scope further in *Union Labor Life Insurance Co. v. Pireno*, 458 U.S. 119 (1982). The *Pireno* case involved an alleged conspiracy to eliminate price competition among chiropractors by means of a committee that advised an insurance company regarding the chiropractor's fees and treatments. The Supreme Court held that the insurance company's use of the committee to render opinions regarding the necessity of chiropractor treatment and the reasonableness of fees did not constitute the "business of insurance" to exempt such a relationship from the scope of the antitrust laws.

The Supreme Court finally enunciated in *Pireno* three criteria relevant in determining whether a particular practice is part of the "business of insurance": first, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry. *Id.* at 129.[7] The *Pireno* court stated further that none of the criteria were "determinative" in and of themselves, but that the practice must be examined in light of all three. *Id.* Though the challenged practice in *Pireno* in essence focused on the claims adjustment process, the Court declined to find that it constituted the "business of insurance."

The Court first stated that the practice was "logically and temporally unconnected to the transfer of risk" accomplished by the insurance policies. *Id.* at 130. Risk is

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including, "the composition of their boards of directors, when their books and records could be inspected, how they could invest their funds, *when they could liquidate* or merge . . . ." *Id.* at 230 n.38 (Emphasis added).

[7] The Supreme Court recently reaffirmed these three criteria in *Metropolitan Life Insurance Co. v. Massachusetts*, ___ U.S. ___, 105 S. Ct. 2380, 2391 (1985).

transferred at the time the contract of insurance is entered into between the insurer and insured and not later when, as in *Pireno,* the insurance company made the decision to pay a claim because it was thereafter determined to be "necessary" or "reasonable." Second, the Court determined that the insurer's use of the committee was not an integral part of the policy relationship between the insurer and insured because the insured has no interest in why his claim is paid but only in whether it is paid. *Id.* at 132. Finally, the Court observed that it was clear that the challenged practice was not confined to the insurance industry itself, but rather involved third parties "wholly outside" it. *Id.* Once again, the Supreme Court held that the challenged practice was not the "business of insurance" and the antitrust exemption of the McCarran-Ferguson Act did not apply.

Other cases decided by the Supreme Court and the lower courts are generally instructive in exemplifying what the "business of insurance" is and what it is not. For example, in *Royal Drug,* the Supreme Court noted that just because an agreement is necessary to provide insurance (such as provider agreements to minimize costs of service benefit insurance plans), it does not follow that it is also the "business of insurance." That an indemnity insurer must have a line of credit or other commercial arrangement with a bank in order to pay off monetary claims and to fulfill its obligations does not convert such an arrangement into the "business of insurance." *Royal Drug,* 440 U.S. at 214 n.9. Premium financing by an insurance company rather than a third party loan or finance company does not constitute the "business of insurance." *Perry v. Fidelity Union Life Insurance Co.,* 606 F.2d 468 (5th Cir. 1979) ("one can hardly claim that the extension of credit is an integral part of the insurance business." *Id.* at 470), *but see Lowe v. Aarco-American, Inc.,* 536 F.2d 1160 (7th Cir. 1976). Diversification of an insurance company into areas of commerce in order to lower the cost of goods or services to

its policyholders would not make such acquisitions the "business of insurance." *Royal Drug*, 440 U.S. at 215.

State laws deemed by the courts to regulate the business of insurance include, for example, those affecting the substantive content of insurance contracts, *Metropolitan Life Insurance Co. v. Massachusetts*, 105 S. Ct. 2380, 2391 (1985) (mandated minimum health benefits laws); the fixing of rates, *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944); the selling and advertising of policies, *FTC v. National Casualty Co.*, 357 U.S. 560 (1958); and the licensing of companies and their agents, *Robertson v. People of State of California*, 328 U.S. 440 (1946).

The pronouncements of the Supreme Court in *Pireno* and *Royal Drug* are absolutely controlling in this area of the law.[8] This Court has unequivocally adopted the so-called "*Pireno* test" used by the Supreme Court to define narrowly the "business of insurance." *Blue Cross and Blue Shield*, 620 F. Supp. 907. Having established a legal framework for the narrow issue presented here, the Court must now characterize the challenged statute in this case within these strictures.

Absolutely crucial to the finding that a statute regulates the "business of insurance" is the concept of risk transfer or spread, as necessitated by the quintessential definition of the term "insurance." Insurance is a "contract whereby, for a stipulated consideration, one party undertakes to compensate the other for loss on a specified subject by specified perils." *Black's Law Dictionary* 721 (5th ed. 1979). The consideration is payment proportionate to the

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[8] Thus, the authorities cited by plaintiff are not in the least persuasive as none analyze the concept of "business of insurance" in light of these Supreme Court cases. *Levy v. Lewis*, 635 F.2d 1960 (2d Cir. 1980); *State of Idaho v. Internal Revenue Service*, ___ F. Supp. ___ (D. Idaho 1987) (Civ. No. 85-1501); *Washburn v. Corcoran*, 643 F. Supp. 554 (S.D.N.Y. 1986).

risk involved. A finding that a challenged state statute involves the transfer or spread of risk will satisfy the first prong of the *Pireno* test.

This Court has held that more than a relationship to risk spreading must be shown to meet the *Pireno* criterion. *Blue Cross and Blue Shield,* 620 F. Supp. at 917 (D. Md. 1985). The party seeking the protection of the McCarran-Ferguson Act must show that the challenged priority scheme is "related positively to underwriting and rate-making." *Id.* That is, the practice of prioritizing claims such that all policyholders, including the United States, are treated similarly must "directly facilitate risk spreading and transfer through the provision of insurance." *Id.*

Plaintiff urges that the statutes specifically providing for liquidation of the insurance company and establishing the various priorities for claimants does reflect the concept of risk in the insurance industry. The risk that an insurance company will become insolvent, however, is not the kind of risk transfer emphasized in *Pireno* and *Royal Drug.* The fact that an insurance company may consider the possibility of insolvency as part of their overhead does not affect the essential obligation of the insurer to the insured as contained in the contract of insurance. The obligation of EICOM under its insurance policies to insure against risks of loss is wholly different from the procedure an insurance company must follow to pay claimants in case of insolvency. The policyholders are concerned with EICOM's recognition of its obligation to cover for their losses rather than the legal mechanisms involved in an insolvency proceeding and priority statute. *See, for example, Langdeau v. United States,* 363 S.W.2d 327, 331 (Tex. Cir. App. 1962) ("This is not a regulation of the insurance business; it is a priority established for a class of creditors of an insurance company").[9]

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[9] The *Langdeau* case too was decided pre-*Royal Drug* and *Pireno.*

Similarly, plaintiff contends that other insurance companies must bear the risk of loss of an insurance company in the form of higher premiums to the Maryland guaranty association (the "Property and Casualty Insurance Guaranty Corporation"), an entity created for the purpose of ensuring payment of claims and avoiding loss caused by the collapse of an insurance company. Md. Ann. Code art. 48A § 504 (1986). The guaranty association pays all valid "covered claims" and is then entitled to file a claim with the receivership for reimbursement. If there are insufficient assets to pay the guaranty association, it bears the risk of loss, rather than the insureds. *Id.* § 508. The funds of the guaranty association consist of premiums assessed against viable insurance companies operating in the state of Maryland. *Id.* § 508. The *Pireno* concept of risk transfer and spreading focuses on the policyholders and not the insurance premiums paid by third party insurance companies. Underwriting and ratemaking is far removed from the policy considerations underlying a state's enactment of a guaranty association. A previous legislative determination that losses would be covered by the guaranty association is "logically and temporally unconnected to the transfer of risk . . . ." *Pireno,* 458 U.S. at 130.

Finally, the Court rejects plaintiff's argument that there can be no transfer of risk until the policy is paid and because the priority statute affects payment of the policy when the company is insolvent, enforcement of the statute transfers the risk. The *Pireno* court, upon examination of an insurance company's claims adjustment process, unequivocally stated that risk is transferred at the time the contract of insurance is entered into.

The "indispensable" first prong of the *Pireno* test has not been met in this case and, therefore, the Court must hold that the process of liquidating an insurance company and fixing the priorities of its claimants is not the "business of insurance" as that term is defined in the McCarran-Ferguson Act. Summary judgment can be granted

in favor of the United States on this ground alone. Plaintiff's assertion that it need only meet one of the three *Pireno* requirements is tenuous in light of the Court's recognition that satisfaction of the first prong of the *Pireno* test, whether the challenged statute facilitates the transfer or spread of risk, is overwhelmingly important. Though the Supreme Court did not make it perfectly clear as to whether all three requirements must be satisfied,[10] the Court finds that failure to show a positive relationship to underwriting and ratemaking is fatal.

In any event, the last two prongs of the *Pireno* test have not been met. The Court finds that neither the liquidation statute nor the priority statute are an "integral part" of the relationship between the insured and the insurer. The contractual liability to pay on a policy of insurance is obviously distinct from the question of who gets paid first. As with the claims adjustment process described in *Pireno,* the concern is whether a claim is paid, not why it is paid. *Pireno,* 458 U.S. at 132. Plaintiff contends that the priority statute does in fact determine whether a policyholder gets paid. The fallacy of plaintiff's argument is in his focus on the sufficiency of assets of the insurance company and its financial ability to pay rather than its liability for risks of loss as embodied in the contract of insurance. Whether the individual policyholder would be entitled to payment was determined when the contract was entered into; that is, when the risk was transferred, and not at the time of payment, if any. In this regard, the Court sees no difference between the claims adjustment

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[10] Of the three criteria relevant in determining whether a particular practice is part of the "business of insurance," the Supreme Court wrote, "[n]one of these criteria is necessarily determinative in itself . . . ." *Pireno,* 458 U.S. at 130. It is also clear that satisfaction of only one of the criteria is not determinative. *Pilot Life Insurance Co. v. Dedeaux,* ___ U.S. ___, 107 S. Ct. 1549, 1555 (1987).

process in *Pireno* and the priority of claims for payment in the Maryland Insurance Code.

Moreover, in the process of liquidating an insurance company and providing for payment of its claimants, the entity is no longer operating as an insurance business at all. The policyholders stand on equal footing with all other claimants in their interest in getting paid. Likewise, the provision of the insurance code providing that employees' wages should be paid first does not constitute the "business of insurance."

Similarly, as to the final prong, it is clear that the liquidation of EICOM and the payment of claims involve entities outside the insurance industry.[11] It is not required that all parties involved in a challenged practice be insurance companies. *Blue Cross and Blue Shield,* 620 F. Supp. at 919. Insolvency and priority statutes, however, are not peculiar to the insurance industry. The appropriate focus of the "business of insurance" analysis is the nature of the activity itself, not the type of business that is conducting it. *Perry v. Fidelity Union Life Insurance Co.,* 606 F.2d at 470. These statutes govern the rights of all creditors, not just policyholders.

Accordingly, the liquidation of an insolvent insurance company and the priority of claims paid thereto does not constitute the "business of insurance" as that term is used in the McCarran-Ferguson Act.

Proffered policy arguments by the plaintiff do not persuade this Court to carve out an exception to the seemingly harsh results in this case.[12] The plaintiff questions

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[11] This Court has noted that this last criterion of the *Pireno* test "should be given less weight than the previous two." *Blue Cross and Blue Shield,* 620 F. Supp. at 918.

[12] Whatever the result of this case, "covered claims" of policyholders will be paid by the Property and Casualty Insurance Guaranty Corporation. It is the guaranty association, as well as policyholders of

the applicability of § 3713 itself and suggests that the original purpose underlying its enactment no longer exists. This Court is not prepared to question the validity of an almost two-hundred year old statute established for precisely the purpose of seeing that the government gets paid. *King v. United States.*, 379 U.S. 329 (1964). Moreover, the Supreme Court has instructed that the priority statute is to be construed liberally in order to effectuate this purpose.[13] *United States v. Emory,* 314 U.S. 423, 426 (1941), *citing Bramwell v. U.S. Fidelity and Guaranty Co.,* 269 U.S. 483, 487 (1926). The United States may rightfully assert its priority under § 3713. Summary judgment will be entered in favor of the defendants. Counsel for defendants shall submit an appropriate Order to the Court in conformity with this opinion within ten days.

August 31, 1987

/s/Walter E. Black, Jr.
Walter E. Black, Jr.
United States District Judge

"uncovered claims," who will bear the loss. "Covered claims" are, generally, those insurance policy contracts issued to residents of the state of Maryland or for the protection of third parties who reside in the state of Maryland. Md. Ann. Code art. 48A, § 505 (1986). The claims of the United States would not be a "covered claim."

[13] The McCarran-Ferguson Act is to be narrowly construed in face of valid federal regulatory interests. *Cochran v. Paco, Inc.,* 606 F.2d 460, 467 (5th Cir. 1979).

15 U.S.C. § 1011-5

§ 1011. Declaration of policy

Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

§ 1012. Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided,* That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

§ 1013. Suspension until June 30, 1948, of application of certain Federal laws; Sherman Antitrust Act applicable to agreements to, or acts of, boycott, coercion, or intimidation

(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal

Trade Commission Act, and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

§ 1014. Applicability of National Labor Relations Act and Fair Labor Standards Act of 1938

Nothing contained in this chapter shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938, or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.

§ 1015. Definition of "State"

As used in this chapter, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, Guam, and the District of Columbia.

31 U.S.C. § 3713

§ 3713. Priority of Government claims

(a)(1) A claim of the United States Government shall be paid first when—

(A) a person indebted to the Government is insolvent and—

(i) the debtor without enough property to pay all debts makes a voluntary assignment of property;

(ii) property of the debtor, if absent, is attached; or

(iii) an act of bankruptcy is committed; or

(B) the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.

(2) This subsection does not apply to a case under title 11.

(b) A representative of a person or an estate (except a trustee acting under title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government.

MD. ANN. CODE art. 48A § 132-164B

§ 132. Definitions.

For the purposes of this subtitle:

(1) *"Impairment"* or *"insolvency."* The capital of a stock insurer or the surplus of a mutual or reciprocal insurer, shall be deemed to be impaired and the insurer shall be deemed to be insolvent, when such insurer is not possessed of assets at least equal to all liabilities and required reserves together with its total issued and outstanding capital stock and minimum surplus if a stock insurer, or the minimum surplus if a mutual or reciprocal insurer, required by this article to be maintained for the kind or kinds of insurance business it is then authorized to transact.

(2) *"Insurer"* means any person, firm, corporation, association or aggregation of persons doing an insurance business and subject to the insurance supervisory authority of, or to liquidation, rehabilitation, reorganization or conservation by the Commissioner or the equivalent insurance supervisory official of another state. An insurer shall also include a corporation operating a nonprofit health service plan under Subtitle 20 of this Code.

(3) *"Delinquency proceedings"* means any proceeding commenced against an insurer pursuant to this subtitle for the purpose of liquidating, rehabilitating, reorganizing or conserving such insurer.

(4) *"State"* means any state of the United States and also the District of Columbia and Puerto Rico.

(5) *"Foreign country"* means territory outside of any state.

(6) *"Domiciliary state"* means the state in which an insurer is incorporated or organized, or in the case of an insurer incorporated or organized in a foreign country, the state in which such insurer, having become authorized to do business in such state, has at the commencement of delinquency proceedings, the largest amount of its assets held in trust and assets held on deposit for the benefit of its policyholders or policyholders and creditors in the United States, and any such insurer is deemed to be domiciled in such state.

(7) *"Ancillary state"* means any state other than a domiciliary state.

(8) *"Reciprocal state"* means any state other than this State in which in substance and effect the provisions of this subtitle are in force, including the provisions requiring that the Commissioner or equivalent insurance supervisory official be the receiver of a delinquent insurer.

(9) *"General assets"* means all property, real, personal, or otherwise, not specifically mortgaged, pledged, deposited or otherwise encumbered for the security or benefit of specified persons or a limited class or classes of persons, and as to such specifically encumbered property the term includes all such property or its proceeds in excess of the amount necessary to discharge the sum or sums secured thereby. Assets held in trust and assets held on deposit for the security or benefit of all policyholders or all pol-

icyholders and creditors in the United States shall be deemed general assets.

(10) *"Preferred claim"* means any claim with respect to which the law of the State or of the United States accords priority of payments from the general assets of the insurer.

(11) *"Special deposit claim"* means any claim secured by a deposit made pursuant to statute for the security or benefit of a limited class or classes of persons, but not including any general assets.

(12) *"Secured claim"* means any claim secured by mortgage, trust deed, pledge, deposit as security, escrow or otherwise, but not including special deposit claim or claims against general assets. The term also includes claims which more than four months prior to the commencement of delinquency proceedings in the state of the insurer's domicile have become liens upon specific assets by reason of judicial process.

(13) *"Receiver"* means receiver, liquidator, rehabilitator or conservator as the context may require.

§ 133. Jurisdiction of delinquency proceedings; venue; exclusiveness of remedy; appeal; substitute conservator, rehabilitator, or receiver.

(1) The circuit courts of the counties are vested in equity with exclusive original jurisdiction of delinquency proceedings under this subtitle, and are authorized to make all necessary and proper orders to carry out the purposes of this subtitle.

(2) The venue of delinquency proceedings against a domestic insurer shall be in the county of the insurer's principal place of business. The venue of such proceedings against foreign and alien insurers shall be in Baltimore City.

(3) Delinquency proceedings pursuant to this subtitle shall constitute the sole and exclusive method of liquidating, rehabilitating, reorganizing or conserving an insurer, and no court shall entertain a petition for the commencement of such proceedings unless the same has been filed in the name of the State at the instance of the Commissioner.

(4) An appeal shall lie to the Court of Special Appeals from an order granting or refusing rehabilitation, liquidation, or conservation, and from every other order in delinquency proceedings having the character of a final order as to the particular portion of the proceedings embraced therein.

(5) On the initial application by the Commissioner for an order appointing him conservator, rehabilitator, or receiver under this subtitle, or at any time during the course of a conservatorship, rehabilitation, or receivership under this subtitle, the court, on its own motion or on the motion of the Commissioner, may issue an order appointing or substituting a person other than the Commissioner as conservator, rehabilitator, or receiver. Any person so appointed shall have the same powers and duties afforded the Commissioner under this subtitle as statutory conservator, rehabilitator, or receiver.

§ 134. Commencement of delinquency proceedings.

The Commissioner shall commence any such proceedings by application to the court for an order directing the insurer to show cause why the relief prayed for should not be granted. After a full hearing pursuant to the terms of such show-cause order, the court shall either deny the application or grant the application, together with such other relief as the nature of the case and the interests of the policyholders, creditors, stockholders, members, subscribers or the public may require.

§ 135. Injunctions.

(1) Upon application by the Commissioner for such an order to show cause, or at any time thereafter, the court may without notice issue an injunction restraining the insurer, its officers, directors, stockholders, members, subscribers, agents and all other persons from the transaction of its business or the waste or disposition of its property until the further order of the court.

(2) The court may at any time during a proceeding under this subtitle issue such injunctions or orders as may be deemed necessary to prevent interference with the Commissioner or the proceeding, or waste of the assets of the insurer, or the commencement or prosecution of any actions, or the obtaining of preferences, judgments, attachments or other liens, or the making of any levy against the insurer or against its assets or any part thereof.

(3) Notwithstanding any other provision of law, no bond shall be required of the Commissioner as a prerequisite for the issuance of any injunction or restraining order pursuant to this section.

§ 136. Grounds for rehabilitation—Domestic insurers.

The Commissioner may apply to the court for an order appointing him as receiver of and directing him to rehabilitate a domestic insurer upon one or more of the following grounds. That the insurer:

(1) Is impaired or insolvent;

(2) Has refused to submit any of its books, records, accounts or affairs to reasonable examination by the Commissioner, his deputy or examiner;

(3) Has concealed or removed records or assets;

(4) Has failed to comply with an order of the Commissioner to make good an impairment of capital or surplus or both;

(5) Has transferred or attempted to transfer substantially its entire property or business, or has entered into any transaction the effect of which is to merge substantially its entire property or business in that of any other insurer without having first obtained the written approval of the Commissioner;

(6) Has wilfully violated its charter or articles of incorporation or any law of this State;

(7) Has an officer, director or manager who has refused to be examined under oath concerning its affairs;

(8) Has been or is the subject of an application for the appointment of a receiver, trustee, custodian, conservator, or sequestrator of the insurer or its property otherwise than pursuant to the provisions of this article whether such appointment has actually been made or not;

(9) Has consented to such an order through a majority of its directors, stockholders, members or subscribers;

(10) Has failed to pay a final judgment rendered against it in this State upon any insurance contract issued or assumed by it, within sixty (60) days after the judgment became final or within sixty (60) days after the time for taking an appeal has expired, or within sixty (60) days after dismissal of an appeal before final termination, whichever date is the later;

(11) Is found, after examination by the Commissioner, to be in such condition that its further transaction of business will be hazardous to its policyholders, bondholders, or to creditors or to the public.

§ 137. Grounds for liquidation—Domestic and alien insurers.

The Commissioner may apply to the court for an order appointing him as receiver (if his appointment as receiver shall not be then in effect) and directing him to liquidate the business of a domestic insurer or of the United States

branch of an alien insurer having trusteed assets in this State, regardless of whether or not there has been a prior order directing him to rehabilitate such insurer if such insurer:

(1) Has ceased transacting business for a period of one year; or

(2) Is an insolvent insurer and has commenced voluntary liquidation or dissolution, or attempts to commence or prosecute any action or proceeding to liquidate its business or affairs, or to dissolve its corporate charter, or to procure the appointment of a receiver, trustee, custodian or sequestrator under any law except this article; or

(3) Is conducting business in a fraudulent manner; or

(4) Is in such condition that further efforts to rehabilitate the insurer, upon any of the grounds specified in § 136 of this subtitle, appear to be futile.

§ 138. Grounds for conservation—Foreign insurers.

The Commissioner may apply to the court for an order appointing him as receiver or ancillary receiver, and directing him to conserve the assets within this State, of a foreign insurer upon any of the following grounds:

(1) Upon any of the grounds specified in § 136 or 137 of this subtitle or

(2) Upon the ground that is property has been sequestrated in its domiciliary sovereignty or in any other sovereignty.

§ 139. Same—Alien insurers.

The Commissioner may apply to the court for an order appointing him as receiver or ancillary receiver, and directing him to conserve the assets within this State, of any alien insurer upon any of the following grounds:

(1) Upon any of the grounds specified in § 136 or 137 of this subtitle;

(2) Upon the ground that the insurer has failed to comply, within the time designated by the Commissioner, with an order made by him to make good an impairment of its trusteed funds; or

(3) Upon the ground that the property of the insurer has been sequestrated in its domiciliary sovereignty or elsewhere.

§ 140. Grounds for ancillary liquidation—Foreign insurers.

The Commissioner may apply to the court for an order appointing him as ancillary receiver of and directing him to liquidate the business of a foreign insurer having assets, business or claims in this State upon the appointment in the domiciliary state of such insurer of a receiver, liquidator, conservator, rehabilitator or other officer by whatever name called for the purpose of liquidating the business of such insurer.

§ 141. Order of rehabilitation; termination of rehabilitation proceedings.

(1) An order to rehabilitate a domestic insurer shall direct the Commissioner forthwith to take possession of the property of the insurer and to conduct the business thereof, and to take such steps toward removal of the causes and conditions which have made rehabilitation necessary as the court may direct.

(2) If at any time the Commissioner deems that further efforts to rehabilitate the insurer would be useless, he may apply to the court for an order of liquidation.

(3) The Commissioner, or any interested person upon due notice to the Commissioner, at any time may apply to the court for an order terminating the rehabilitation proceedings and permitting the insurer to resume possession of its property and the conduct of its business, but no such order shall be made or entered except when, after

a hearing, the court has determined that the purposes of the proceeding have been fully accomplished.

§ 142. Order of liquidation and order of dissolution—Domestic insurers.

(1) An order to liquidate the business of a domestic insurer shall direct the Commissioner forthwith to take possession of the property of the insurer, to liquidate its business, to deal with the insurer's property and business in his own name as Commissioner or in the name of the insurer, as the court may direct, and to give notice to all creditors who may have claims against the insurer to present such claims.

(2) The Commissioner may apply for and secure an order dissolving the corporate existence of a domestic insurer upon his application for an order of liquidation of such insurer or at any time after such order has been granted.

§ 143. Order of liquidation—Alien insurers.

An order to liquidate the business of a United States branch of an alien insurer having trusteed assets in this State shall be in the same terms as those prescribed for domestic insurers, save and except only that the assets of the business of such United States branch shall be the only assets included therein.

§ 144. Order of conservation or ancillary liquidation of foreign or alien insurers.

(1) An order to conserve the assets of a foreign or alien insurer shall require the Commissioner forthwith to take possession of the property of the insurer within this State and to conserve it, subject to the further direction of the court.

(2) An order to liquidate the assets in this State of a foreign insurer shall require the commissioner forthwith to take possession of the property of the insurer within

this State and to liquidate it subject to the orders of the court and with due regard to the rights and powers of the domiciliary receiver, as provided in this subtitle.

§ 145. Conduct of delinquency proceedings against domestic and alien insurers.

(1) *Appointment of Commissioner as receiver.*—Whenever under this subtitle a receiver is to be appointed in delinquency proceedings for a domestic or alien insurer, the court shall appoint the Commissioner as such receiver. The court shall order the Commissioner forthwith to take possession of the assets of the insurer and to administer the same under the orders of the court.

(2) *Title of Commissioner to assets of insurer.*—As a domiciliary receiver, the Commissioner shall be vested by operation of law with the title to all of the property, contracts and rights of action, and all of the books and records of the insurer, wherever located, as of the date of entry of the order directing him to rehabilitate or liquidate a domestic insurer or to liquidate the United States branch of an alien insurer domiciled in this State, and he shall have the right to recover the same and reduce the same to possession; except that ancillary receivers in reciprocal states shall have, as to assets located in their respective states, the rights and powers which are herein prescribed for ancillary receivers appointed in this State.

(3) *Recording of order directing possession to be taken.*—The filing or recording of the order directing possession to be taken, or a certified copy thereof, in any office where instruments affecting title to property are required to be filed or recorded shall impart the same notice as would be imparted by a deed, bill of sale, or other evidence of title duly filed or recorded.

(4) *Commissioner responsible for administration of assets: bond.*—The Commissioner as domiciliary receiver shall be responsible for the proper administration of all assets

coming into his possession or control. The court may at any time require a bond from him or his deputy if deemed desirable for the protection of such assets.

(5) *Duties of receiver upon taking possession of assets.*—Upon taking possession of the assets of an insurer, the domiciliary receiver shall, subject to the direction of the court, immediately proceed to conduct the business of the insurer or to take such steps as are authorized by this subtitle for the purpose of rehabilitating, liquidating or conserving the affairs or assets of the insurer.

(6) *Deputy commissioners and other personnel.*—In connection with delinquency proceedings, the Commissioner may appoint one or more special deputy commissioners to act for him and he may employ such counsel, clerks and assistants as he deems necessary. The compensation of the special deputies, counsel, clerks or assistants and all expenses of taking possession of the insurer and of conducting the proceedings shall be fixed by the receiver, subject to the approval of the court, and shall be paid out of the funds or assets of the insurer. Within the limits of duties imposed upon them, special deputies shall possess all the powers given to and, in the exercise of those powers, shall be subject to all of the duties imposed upon the receiver with respect to such proceedings.

§ 146. Conduct of delinquency proceedings against foreign insurers.

(1) *Appointment of Commissioner as ancillary receiver.*—Whenever under this subtitle an ancillary receiver is to be appointed in delinquency proceedings for an insurer not domiciled in this State, the court shall appoint the Commissioner as ancillary receiver. The Commissioner shall file a petition requesting the appointment on the grounds set forth in § 140 of this subtitle:

(i) If he finds that there are sufficient assets of the insurer located in this State to justify the appointment of an ancillary receiver; or

(ii) If ten or more persons resident in this State having claims against such insurer file a petition with the Commissioner requesting the appointment of such ancillary receiver.

(2) *Rights, powers and duties of domiciliary and ancillary receivers.*—The domiciliary receiver for the purpose of liquidating an insurer domiciled in a reciprocal state shall be vested by operation of law with the title to all of the property, contracts and rights of action, and all of the books and records of the insurer located in this State, and he shall have the immediate right to recover balances due from local agents and to obtain possession of any books and records of the insurer found in this State. He shall also be entitled to recover the other assets of the insurer located in this State, except that upon the appointment of an ancillary receiver in this State, the ancillary receiver shall during the ancillary receivership proceedings have the sole right to recover such other assets. The ancillary receiver shall, as soon as practicable, liquidate from their respective securities those special deposit claims and secured claims which are proved and allowed in the ancillary proceedings in this State, and shall pay the necessary expenses of the proceedings. All remaining assets he shall promptly transfer to the domiciliary receiver. Subject to the foregoing provisions, the ancillary receiver and his deputies shall have the same powers and be subject to the same duties with respect to the administration of such assets as a receiver of an insurer domiciled in this State.

(3) *Suits by domiciliary receiver.*—The domiciliary receiver of an insurer domiciled in a reciprocal state may sue in this State to recover any assets of such insurer to which he may be entitled under the laws of this State.

§ 147. Claims of nonresidents against domestic insurers.

(1) *Filing of claims.*—In a delinquency proceeding begun in this State against a domestic insurer, claimants residing

in reciprocal states may file claims either with the ancillary receivers, if any, in their respective states, or with the domiciliary receiver. All such claims must be filed on or before the last date fixed for the filing of claims in the domiciliary delinquency proceedings.

(2) *Proof of claims.*—Controverted claims belonging to claimants residing in reciprocal states may either:

(i) Be proved in this State; or

(ii) If ancillary proceedings have been commenced in such reciprocal states, may be proved in those proceedings. In the event a claimant elects to prove his claim in ancillary proceedings, if notice of the claim and opportunity to appear and be heard is afforded the domiciliary receiver of this State, as provided in § 148 of this subtitle with respect to ancillary proceedings in this State, the final allowance of such claim by the courts in the ancillary state shall be accepted in this State as conclusive as to its amount and shall also be accepted as conclusive as to its priority, if any, against special deposits or other security located within the ancillary state.

§ 148. Claims of residents of this State against foreign insurers.

(1) *Filing of claims.*—In a delinquency proceeding in a reciprocal state against an insurer domiciled in that state, claimants against such insurer who reside within this State may file claims either with the ancillary receiver, if any, appointed in this State, or with the domiciliary receiver. All such claims must be filed on or before the last date fixed for the filing of claims in the domiciliary delinquency proceedings.

(2) *Proof of claims.*—Controverted claims belonging to claimants residing in this State may either:

(i) Be proved in the domiciliary state as provided by the law of that state; or

(ii) If ancillary proceedings have been commenced in this State, be proved in those proceedings. In the event that any such claimant elects to prove his claim in this State, he shall file his claim with the ancillary receiver and shall give notice in writing to the receiver in the domiciliary state, either by certified mail, return receipt requested, bearing a postmark from the United States Postal Service, or by personal service at least forty days prior to the date set for hearing. The notice shall contain a concise statement of the amount of the claim, the facts on which the claim is based, and the priorities asserted, if any. If the domiciliary receiver within thirty days after the giving of such notice shall give notice in writing to the ancillary receiver and to the claimant, either by certified mail, return receipt requested, bearing a postmark from the United States Postal Service, or by personal service, of his intention to contest such claim, he shall be entitled to appear or to be represented in any proceeding in this State involving adjudication of the claim. The final allowance of the claim by the courts of this State shall be accepted as conclusive as to its amount and shall also be accepted as conclusive as to its priority, if any, against special deposits or other security located within this State.

§ 149. Form of claim; notice; hearing; allowance or disallowance of claim.

(1) *Form of claim.*—Claimants shall set forth in reasonable detail the amount of the claim, or the basis upon which such amount can be ascertained, the facts upon which the claim is based, and the priorities asserted, if any. All such claims shall be verified by the affidavit of the claimant, or someone authorized to act on his behalf and having knowledge of the facts, and shall be supported by such documents as may be material thereto.

(2) *How and when filed.*—All claims filed in this State shall be filed with the receiver, whether domiciliary or

ancillary, in this State, on or before the last date for filing as specified in this subtitle.

(3) *Report and recommendation of receiver; notice of hearing.*—Within ten days of the receipt of any claim, or within such further period as the court may, for good cause shown, fix, the receiver shall report the claim to the court, specifying in such report his recommendation with respect to the action to be taken thereon. Upon receipt of such report, the court shall fix a time for hearing the claim and shall direct that the claimant or the receiver, as the court shall specify, shall give such notice as the court shall determine to such persons as shall appear to the court to be interested therein. All such notices shall specify the time and place of the hearing and shall concisely state the amount and nature of the claim, the priorities asserted, if any, and the recommendation of the receiver with reference thereto.

(4) *Hearing and order.*—At the hearing, all persons interested shall be entitled to appear and the court shall enter an order allowing, allowing in part, or disallowing the claim. Any such order shall be deemed to be an appealable order.

§ 150. Priority of certain claims.

(1) *Claims of residents of ancillary states.*—In a delinquency proceeding against an insurer domiciled in this State, claims owing to residents of ancillary states shall be preferred claims if like claims are preferred under the laws of this State. All such claims owing to residents or nonresidents shall be given equal priority of payment from general assets regardless of where such assets are located.

(2) *Claims against insurer domiciled in reciprocal state.*—In a delinquency proceeding against an insurer domiciled in a reciprocal state, claims owing to residents of this State shall be preferred if like claims are preferred by the laws of that state.

(3) *Special deposit claims.*—The owners of special deposit claims against an insurer for which a receiver is appointed in this or any other state shall be given priority against their several special deposits in accordance with the provisions of the statutes governing the creation and maintenance of such deposits. If there is a deficiency in any such deposit so that the claims secured thereby are not fully discharged therefrom, the claimants may share in the general assets, but such sharing shall be deferred until general creditors, and also claimants against other special deposits who have received smaller percentages from their respective special deposits, have been paid percentages of their claims equal to the percentage paid from the special deposit.

(4) *Secured claims.*—The owner of a secured claim against an insurer for which a receiver has been appointed in this or any other state may surrender his security and file his claim as a general creditor, or the claim may be discharged by resort to the security, in which case the deficiency, if any, shall be treated as a claim against the general assets of the insurer on the same basis as claims of unsecured creditors. If the amount of the deficiency has been adjudicated in ancillary proceedings as provided in this subtitle, or if it has been adjudicated by a court of competent jurisdiction in proceedings in which the domiciliary receiver has had notice and opportunity to be heard, such amounts shall be conclusive; otherwise the amount shall be determined in the delinquency proceeding in the domiciliary state.

§ 151. Attachment and garnishment of assets.

During the pendency of delinquency proceedings in this or any reciprocal state, no action or proceeding in the nature of an attachment, garnishment or execution shall be commenced or maintained in the courts of this State against the delinquent insurer or its assets. Any lien obtained or any such action or proceeding within four months

prior to the commencement of any such delinquency proceeding or at any time thereafter shall be void as against any rights arising in such delinquency proceeding.

§ 152. Sections constituting Uniform Insurers Liquidation Act; construction.

(1) Paragraphs (2) to (13) inclusive, of § 132, together with §§ 145, 146, 147, 148, 150 and 151 constitute and may be referred to as the "Uniform Insurers Liquidation Act."

(2) The Uniform Insurers Liquidation Act shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states that enact it. To the extent that its provisions when applicable conflict with other provisions of this subtitle, the provisions of such act shall control.

§ 153. Deposit of money collected; investment in shares of savings and loan or building and loan associations.

(a) The moneys collected by the Commissioner in a proceeding under this subtitle shall be from time to time deposited in one or more State or national banks, savings banks or trust companies, and in the case of the insolvency or voluntary or involuntary liquidation of any such depository which is an institution organized and supervised under the laws of this State, such deposits shall be entitled to priority of payment on an equality with any other priority given by the banking laws of this State. The Commissioner may in his discretion deposit such moneys or any part thereof in a national bank or trust company as a trust fund.

(b) To the extent that such an investment or account is insured by the Federal Savings and Loan Insurance Corporation or by the Maryland Savings-Share Insurance Corporation, the Commissioner may invest in shares of

savings and loan associations or building and loan associations.

§ 154. Exemption from fees.

The Commissioner shall not be required to pay any fee to any public officer in this State for filing, recording, issuing a transcript or certificate or authenticating any paper or instrument pertaining to the exercise by the Commissioner of any of the powers or duties conferred upon him under this subtitle, whether or not such paper or instrument be executed by the Commissioner or his deputies, employees or attorneys of record and whether or not it is connected with the commencement of any action or proceeding by or against the Commissioner, or with the subsequent conduct of such action or proceeding.

Nothing herein contained, however, shall be taken to relieve the Commissioner or his deputy, acting as receiver, ancillary receiver, conservator, etc. pursuant to the terms of this subtitle, from the payment of all court costs out of the assets of the insurer prior to any distribution to creditors or termination of rehabilitation. In all such cases the costs, including those contained in paragraph one hereof, shall be charged in the Commissioner's accounts to the court or be paid by the insurer as a condition of termination of the proceedings, as the case may be.

§ 155. Borrowing and pledge of assets.

For the purpose of facilitating the rehabilitation, liquidation, conservation or dissolution of an insurer pursuant to this subtitle, the Commissioner may, subject to the approval of the court, borrow money and execute, acknowledge and deliver the notes or other evidences of indebtedness therefor and secure the repayment of the same by the mortgage, pledge, assignment, transfer in trust, or hypothecation of any or all of the property, whether real, personal or mixed, of such insurer, and the Commissioner subject to the approval of the court shall

have power to take any and all other action necessary and proper to consummate any such loan and to provide for the repayment thereof. The Commissioner shall be under no obligation personally or in his official capacity to repay any loan made pursuant to this section.

§ 156. Date rights fixed on liquidation.

The rights and liabilities of the insurer and of its creditors, policyholders, stockholders, members, subscribers and all other persons interested in its estate shall, unless otherwise directed by the court, be fixed as of the date on which the order directing the liquidation of the insurer is filed in the office of the clerk of the court which made the order, subject to the provisions of this subtitle with respect to the rights of claimants holding contingent claims.

§ 157. Voidable transfers.

(1) *Certain transfers voidable.*—Any transfer of, or lien upon, the property of an insurer which is made or created within four months prior to the granting of an order to show cause under this subtitle with the intent of giving to any creditor a preference or of enabling him to obtain a greater percentage of his debt than any other creditor of the same class and which is accepted by such creditor having reasonable cause to believe that such preference will occur, shall be voidable.

(2) *Liability of persons concerned in such transfers.*—Every director, officer, employee, stockholder, member, subscriber and any other person acting on behalf of such insurer who shall be concerned in any such act or deed and every person receiving thereby any property of such insurer or the benefit thereof shall be personally liable therefor and shall be bound to account to the Commissioner.

(3) *Avoidance of transfer and recovery of property or its value.*—The Commissioner as receiver in any proceeding under this subtitle may avoid any transfer of or lien upon

the property of an insurer which any creditor, stockholder, subscriber or member of such insurer might have avoided and may recover the property so transferred unless such person was a bona fide holder for value prior to the date of the entering of an order to show cause under this subtitle. Such property or its value may be recovered from anyone who has received it except a bona fide holder for value as herein specified.

§ 158. Priority of claims for compensation.

(a) Compensation actually owing to officers and employees of an insurer, for services rendered within three months prior to the commencement of a proceeding against the insurer under this subtitle, but not exceeding five hundred dollars ($500) for each officer or employee, shall be paid prior to the payment of any other debt or claim, and in the discretion of the Commissioner may be paid as soon as practicable after the proceeding has been commenced; except that at all times the Commissioner shall reserve such funds as will in his opinion be sufficient for the expenses of administration.

(b) Such priority shall be in lieu of any other similar priority which may be authorized by law as to wages or compensation of such employees.

§ 158A. Priority of claims other than administration expenses, wages and taxes.

Claims by policyholders, beneficiaries, and insureds arising from and within the coverage of and not in excess of the applicable limits of insurance policies and insurance contracts issued by the company, and liability claims against insureds which claims are within the coverage of and not in excess of the applicable limits of insurance policies and insurance contracts issued by the company, and claims of the Property and Casualty Insurance Guaranty Corporation and the Maryland Life and Health Insurance Guaranty Association and any similar organization

in another state shall have priority in a liquidation proceeding over all other claims except those for expenses of administration, wages covered by § 158 and taxes.

§ 159. Offsets.

(a) In all cases of mutual debts and credits between the insurer and another person in connection with any action or proceeding under this subtitle, such debts and credits shall be set off and the balance only shall be allowed or paid, except as provided in subsection (b) below.

(b) No offset shall be allowed in favor of any such person where:

(1) The obligation of the insurer to such person would not at the date of the entry of any liquidation order or otherwise, as provided in § 156, entitle him to share as a claimant in the assets of the insurer; or

(2) The obligation of the insurer to such person was purchased by or transferred to such person with a view of its being used as an offset; or

(3) The obligation of such person is to pay an assessment levied against the members of a mutual insurer, or against the subscribers of a reciprocal insurer, or is to pay a balance upon the subscription to the capital stock of a stock insurer.

§ 160. Allowance of certain claims.

(a) *Contingent and unliquidated claims generally.*—No contingent and unliquidated claim shall share in a distribution of the assets of an insurer which has been adjudicated to be insolvent by an order made pursuant to this subtitle, except that such claim shall be considered, if properly presented, and may be allowed to share where:

(1) Such claim becomes absolute against the insurer on or before the last day for filing claims against the assets of such insurer; or

(2) There is a surplus and the liquidation is thereafter conducted upon the basis that such insurer is solvent.

(b) *Claims under liability insurance policies.*—Where an insurer has been so adjudicated to be insolvent any person who has a cause of action against an insured of such insurer under a liability insurance policy issued by such insurer shall have the right to file a claim in the liquidation proceeding, regardless of the fact that such claim may be contingent, and such claim may be allowed:

(1) If it may be reasonably inferred from the proof presented upon such claim that such person would be able to obtain a judgment upon such cause of action against such insured; and

(2) If such person shall furnish suitable proof, unless the court for good cause shown shall otherwise direct, that no further valid claim against such insurer arising out of his cause of action other than those already presented can be made; and

(3) If the total liability of such insurer to all claimants arising out of the same act of its insured shall be no greater than its maximum liability would be were it not in liquidation.

(c) *Same—Certain judgments against insured not taken as evidence of liability.*—No judgment against such an insured taken after the date of entry of the liquidation order shall be considered in the liquidation proceedings as evidence of liability, or of the amount of damages, and no judgment against an insured taken by default, or by collusion prior to the entry of the liquidation order shall be considered as conclusive evidence in the liquidation proceedings, either of the liability of such insured to such person upon such cause of action or of the amount of damages to which such person is therein entitled.

(d) *Claims of secured claimants.*—No claim of any secured claimant shall be allowed at a sum greater than the

difference between the value of the claim without security and the value of the security itself as of the date of the entry of the order of liquidation or such other date set by the court for determining rights and liabilities as provided in § 156 unless the claimant shall surrender his security to the Commissioner, in which event the claim shall be allowed in the full amount for which it is valued.

§ 161. Order of insolvency; time for filing claims after entry of such order.

(a) If upon the entry of an order of liquidation under this subtitle or at any time thereafter during liquidation proceedings the insurer shall not be clearly solvent, the court shall, upon hearing after such notice it deems proper, make and enter an order adjudging the insurer to be insolvent.

(b) After the entry of the order of insolvency, regardless of any prior notice that may have been given to creditors, the Commissioner shall notify all persons who may have claims against such insurer to file such claims with him, at a place and within the time specified in the notice, or that such claims shall be forever barred. The time specified in the notice shall be as fixed by the court for filing of claims and which shall be not less than six (6) months after the entry of the order of insolvency. The notice shall be given in such manner and for such reasonable period of time as may be ordered by the court.

§ 162. Report of Commissioner and petition for assessment.

Within three years after the date of the entry of an order of rehabilitation or liquidation of a domestic mutual insurer or a domestic reciprocal insurer, the Commissioner may take and file his report and petition to the court setting forth:

(a) The reasonable value of the assets of the insurer;

(b) The liabilities of the insurer to the extent thus far ascertained by the Commissioner;

(c) The aggregate amount of the assessment, if any, as provided in § 260 (a), which the Commissioner deems reasonably necessary to pay all claims, the costs and expenses of the collection of the assessments and the costs and expenses of the delinquency proceedings in full;

(d) Any other information relative to the affairs or property of the insurer that the Commissioner deems material.

§ 162A. Disbursement of assets to insurance guaranty associations.

(a) *Application for approval of proposal to disburse.*—Within 120 days of a final determination of insolvency of a company by a court of competent jurisdiction of this State, the Commissioner as receiver shall make application to the court for approval of a proposal to disburse unsecured assets out of the company's marshalled assets, from time to time as such assets become available, to the Property and Casualty Insurance Guaranty Corporation and the Maryland Life and Health Insurance Guaranty Association and to any similar organization in another state. (The Property and Casualty Insurance Guaranty Corporation and the Maryland Life and Health Guaranty Association and any similar organizations in other states shall hereinafter be referred to collectively as the "associations.")

(b) *Required provisions in proposal.*—The proposal shall at least include provision for:

(1) Adequate cash reserves for the payment of the expenses of administration and priority claims;

(2) Disbursements of the assets marshalled to date and subsequent disbursements of assets as they become available;

(3) Equitable allocation of disbursements to each of the associations entitled thereto; and

(4) The securing by the Commissioner from each of the associations entitled to disbursements pursuant to this section and agreement to return to the Commissioner such assets previously disbursed as may be required to pay claims of secured creditors and claims falling within the priorities established in § 158 (a) of this article in accordance with the priorities. No bond shall be required of any association.

(c) *Amount of disbursements.*—The Commissioner's proposal shall provide for disbursements to the associations in amounts at least equal to the payments made or to be made thereby for which these associations could assert claims against the Commissioner, and shall further provide that if the assets available for disbursement from time to time do not equal or exceed the amount of the payments made or to be made by the associations then disbursements shall be in the amount of available assets.

(d) *Notice to associations.*—Notice of the application shall be given to the associations in and to the commissioners of insurance of each of the states. Any notice shall be deemed to have been given when deposited in the United States certified mails, first-class postage prepaid, at least 30 days prior to submission of such application to the court. Action on the application may be taken by the court provided the above required notice has been given and provided further that the Commissioner's proposal complies with subsection (b) (1) and (b) (4).

§ 163. Order and levy of assessment.

(a) *Order of assessment.*—Upon the filing and reading of the report and petition provided for in § 162, the court, ex parte, may order the Commissioner to assess all members or subscribers of the insurer who may be subject to such an assessment, in such an aggregate amount as the court finds reasonably necessary to pay all valid claims as may be timely filed and proved in the delinquency proceedings, together with the costs and expenses of levying

and collecting assessments and the costs and expenses of the delinquency proceedings in full. Any such order shall require the Commissioner to assess each such member or subscriber for his proportion of the aggregate assessment, according to such reasonable classification of such members or subscribers and formula as may be made by the Commissioner and approved by the court.

(b) *Additional assessments.*—The court may order additional assessments to all members or subscribers of the insurer who may be subject to such an assessment, upon the filing and reading of any amendment or supplement to the report and petition referred to in subsection (a) above, if such amendment or supplement is filed within three (3) years after the date of the entry of the order of rehabilitation or liquidation.

(c) *Commissioner to levy assessment in accordance with order.*—After the entry of the order to levy and assess members or subscribers of an insurer referred to in (a) or (b) above, the Commissioner shall levy and assess members or subscribers in accordance with the order.

(d) *Maximum total assessments.*—The total of all assessments against any member or subscriber with respect to any policy, whether levied pursuant to this subtitle or pursuant to any other provision of this article, shall be for no greater amount than that specified in the policy or polices of the member or subscriber and as limited under this article.

(e) *No assessment with respect to nonassessable policy.*—No assessment shall be levied against any member or subscriber with respect to any nonassessable policy issued in accordance with this article.

§ 164. Assessment prima facie correct; notice; payment; proceedings to collect.

(a) *Assessment prima facie correct.*—Any assessment of a subscriber or member of an insurer made by the Com-

missioner pursuant to the order of court fixing the aggregate amount of the assessment against all members or subscribers and approving the classification and formula made by the Commissioner under § 163 shall be prima facie correct.

(b) *Notice.*—Each member or subscriber shall be notified of the amount of assessment to be paid by him by written notice mailed to the address of the member or subscriber last of record with the insurer. Failure of the member or subscriber to receive the notice so mailed, within the time specified therein for the payment of the assessment or at all, shall be no defense in any proceeding to collect the assessment.

(c) *Commencement of proceedings to collect.*—If any such member or subscriber fails to pay the assessment within the period specified in the notice, which period shall not be less than twenty (20) days after mailing, the Commissioner may obtain an order in the delinquency proceedings requiring the member or subscriber to show cause at a time and place fixed by the court why judgment should not be entered against such member or subscriber for the amount of the assessment together with all costs, and a copy of the order and a copy of the petition therefor shall be served upon the member or subscriber within the time and in the manner designated in the order.

(d) *Judgment in proceedings to collect.*—If the subscriber or member after due service of a copy of the order and petition referred to in (c) above is made upon him:

(1) Fails to appear at the time and place specified in the order, judgment shall be entered against him as prayed for in the petition; or

(2) Appears in the manner and form required by law in response to the order, the court shall hear and determine the matter and enter a judgment in accordance with its decision.

(e) *Collection by other means.*—The Commissioner may collect any such assessment through any other lawful means.

§ 164A. Notice of delinquency proceedings to be given to policyholders.

The receiver or conservator of any company against which delinquency proceedings are instituted under this subtitle shall within fifteen (15) days after his appointment as receiver or conservator notify each policyholder of the company by letter or such other means as the circuit courts may approve of the institution of the delinquency proceedings and of the possibility of the future cancellation of his insurance.

§ 164B. Immunity in receivership proceedings.

(a) *Certain officers immuned from liability.*—No claim of any nature whatsoever that is directly related to the receivership of an insurer shall arise against, and no liability shall be imposed upon, the Insurance Commissioner, Deputy Commissioner, Special Deputy Commissioner, or any person or entity acting as a receiver of an insurer, including surety, in rehabilitation, liquidation, or conservation as a result of a court order issued on or after January 1, 1985 for any statement made or actions taken or not taken in the good faith exercise of their powers under law. However this immunity shall not extend to acts or omissions which are malicious or grossly negligent. This qualified immunity extends to agents and employees of the receiver.

(b) *Representation of special deputy commissioners*—In any civil proceeding filed against a Special Deputy Commissioner appointed pursuant to this subtitle, the Special Deputy Commissioner shall be entitled to representation by the Attorney General in accordance with § 12-304 through § 12-312 of the State Government Article.

MD. ANN. CODE art. 48A § 504-19

§ 504. Purposes and scope of subtitle.

(a) *Purpose.*—(1) The purposes of this subtitle are to provide a mechanism for the prompt payment of covered claims under certain insurance policies and to avoid financial loss to residents of Maryland who are claimants or policyholders of an insurer, including surety, which has become insolvent; and to provide for the assessment of the cost of such payments and protection among insurers.

(2) All provisions of this subtitle shall apply to any insurer insolvency, including surety, existing as of January 1, 1985.

(b) *Scope.*—This subtitle shall apply to all kinds of direct insurance, except life insurance, health insurance, and annuities. On July 1, 1975 all of the assets and obligations of every type and description of the Motor Vehicle Security Fund as of the close of business on June 30, 1975 shall be transferred to the Property and Casualty Insurance Guaranty Corporation and administered through the appropriate account under § 506 of this subtitle. On July 1, 1981, all the assets and obligations of every type and description of the Workmen's Compensation Insolvency Fund at the close of business on June 30, 1981 shall be transferred to the Property and Casualty Insurance Guaranty Corporation and administered through the appropriate account under § 506 of this subtitle.

§ 505. Definitions.

As used in this subtitle:

(a) *"Account"* means any one of the four accounts created by § 506 of this subtitle.

(b) *"Association"* means the Property and Casualty Insurance Guaranty Corporation created under § 506 of this subtitle.

(c) (1) *"Covered claims"* means obligations, including unearned premiums, of an insolvent insurer which:

(i) 1. Arise out of the insurance policy contracts of the insolvent insurer issued to residents of this State or which are payable to residents of this State on behalf of insureds of the insolvent insurer; or

2. Arise out of surety bonds issued by the insolvent insurer for the protection of third parties, who are residents of this State;

(ii) Were unpaid by the insolvent insurer;

(iii) Are presented as a claim to the receiver in this State or the Association on or before the last date fixed for the filing of claims in the domiciliary delinquency proceedings;

(iv) 1. Except for surety bond claims, were incurred or existed prior to, on, or within 30 days after the determination of insolvency; or

2. For surety bond claims arising under surety bonds issued by a domestic insurer were incurred or existed prior to, on, or within 18 months after the determination of insolvency, whether or not the surety bonds are issued for no stated period or for a stated period; and

(v) Arise out of policy contracts or surety bonds of the insolvent insurer issued for the kinds of insurance to which this subtitle applies.

(2) "Covered claim" does not include any amount due any reinsurer, insurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise. No insurer shall assert a claim of subrogation against an insured of an insolvent insurance company but may assert any claim it may have against the receiver of the insolvent insurance company.

(d) *"Insolvent insurer"* means:

(1) An insurer authorized to transact insurance or authorized to issue surety bonds in this State either at the time the policy or surety bond was issued or when the event giving rise to the claim occurred; and

(2) Against whom a final order of liquidation, with a finding of insolvency, has been entered by a court of competent jurisdiction in the state of domicile of the insurer.

(e) (1) *"Member insurer"* means any insurer which:

(i) Writes any kind of insurance to which this subtitle applies under § 504 of this subtitle including the exchange of reciprocal or interinsurance contracts; and

(ii) Is licensed to transact insurance in this State.

(2) "Member insurer" includes the Maryland Automobile Insurance Fund.

(f) (1) *"Net direct written premiums"* means direct gross premiums written in this State on insurance policies or surety bonds to which this subtitle applies, less return premiums thereon and dividends paid or credited to policyholders, or principals or obligees of surety bonds on such direct business.

(2) "Net direct written premiums" does not include premiums on contracts between insurers or reinsurers, or premiums received by insurers under the Maryland Property Insurance Availability Act.

(g) (1) *"Surety bond"*, *"surety"*, and *"suretyship"* mean insurance that guarantees the performance of contracts, other than insurance policies, and guarantee and execute bonds, undertakings, and contracts of suretyship.

(2) "Surety bond", "surety", and "suretyship" do not include mortgage guaranty, financial guaranty, or other forms of insurance offering protection against investment risks.

(h) *"Resident"* means:

(l) An individual domiciled in this State;

(2) In the case of a corporation or other entity that is not a natural person, a corporation or entity whose principal place of business is in this State.

§ 506. Corporation created; membership; division into separate accounts.

(a) *Creation.*—There is created a private, nonprofit, nonstock corporation which shall be known as the Property and Casualty Insurance Guaranty Corporation.

(b) *Members.*—All insurers defined as member insurers in § 505 (e) of this subtitle shall be and remain members of the Corporation as a condition of their authority to transact insurance in this State.

(c) *Plan of operation: directors.*—The Corporation shall perform its functions under a plan of operation established and approved under § 509 of this subtitle and shall exercise its powers through a board of directors established under § 507 of this subtitle.

(d) *Accounts.*—For purposes of administration and assessment, the Corporation shall be divided into four separate accounts: (1) the title insurance account; (2) the motor vehicle insurance account; (3) the workmen's compensation account; and (4) the account for all other insurance to which this subtitle applies.

(e) *Powers, privileges and immunities of corporation.*—Except as otherwise provided in this subtitle, the Corporation has all the powers, privileges, and immunities including perpetual existence, granted by the applicable provisions of the Corporations and Associations Article.

(f) *Corporation not deemed department, unit, agency, etc. of State.*—The Corporation is not and may not be deemed a department, unit, agency, or instrumentality of the State for any purpose. All debts, claims, obligations, and liabilities of the Corporation, whenever incurred, shall be the

debts, claims, obligations, and liabilities of the Corporation only and not of the State, its agencies, instrumentalities, officers, or employees. The Corporation moneys may not be considered part of the General Fund of the State. The State may not budget for or provide General Fund appropriations to the Corporation, and the debts, claims, obligations, and liabilities of the Corporation may not be considered to be a debt of the State or a pledge of its credit.

§ 507. Board of directors.

(a) *Composition; appointment and terms of members; chairman; vacancies.*—The board of directors of the Corporation shall consist of not less than five nor more than nine persons serving terms as established in the plan of operation. The members of the board shall be elected from member insurers. Vacancies of the board shall be filled for the remaining period of the term by a majority vote of the remaining members of the board. A chairman shall be elected by the board from its members. The board may elect officers and shall appoint an executive committee of three from its members.

(b) *Fair representation of member insurers.*—In electing directors or filling vacancies on the board, consideration shall be given to, among other things, whether all member insurers are fairly represented.

(c) *Reimbursement for expenses.*—Members of the board may be reimbursed from the assets of the Corporation for expenses incurred by them as members of the board of directors.

§ 508. Powers and duties of Corporation.

(a) The Corporation shall:

(1) (i) Except as to surety bonds, be obligated to the extent of the covered claims existing prior to the determination of insolvency and arising within 30 days after

the determination of insolvency, or before the policy expiration date if less than 30 days after the determination, or before the insured replaces the policy or causes its cancellation, if he does so within 30 days of the determination, but such obligation shall include only that amount of each covered claim which is in excess of $100 and less than $300,000. However, the Association shall pay the full amount of any covered claim arising out of a workmen's compensation policy. In no event shall the Corporation be obligated to a policyholder or claimant in an amount in excess of the obligation of the insolvent insurer under the policy from which the claim arises.

(ii) With respect to surety bonds, be obligated to the extent of the covered claims existing prior to the determination of insolvency, and arising within 18 months after the determination of insolvency whether or not the surety bonds are issued with no stated period or for a stated period. Such obligation shall include only that amount of each covered claim payable to each claimant which is in excess of $100 and less than $300,000. In no event shall the Association be liable for an aggregate amount in excess of $1,000,000 under any one bond. In the event covered claims are in excess of $1,000,000 under any one bond, the Association shall make a prorated payment on account of each covered claim in the ratio that the covered claim bears to the total amount of all covered claims under the bond. In no event shall the Association be obligated to any claimants in an amount in excess of the obligation of the insolvent insurer under the surety bond from which the claim arises.

(2) Be deemed the insurer to the extent of its obligation on the covered claims and to such extent shall have all rights, duties, and obligations of the insolvent insurer as if the insurer had not become insolvent.

(3) Allocate claims paid and expenses incurred among the four accounts separately, and assess member insurers

separately for each account in amounts necessary to pay the obligation of the Corporation under paragraph (1) of this subsection subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, and other expenses authorized by this subtitle. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding calendar year on the kinds of insurance in the account bears to the net direct written premiums of all member insurers for the preceding calendar year on the kinds of insurance in the account. Each member insurer shall be notified of the assessment not later than 30 days before it is due. No member insurer may be assessed in any year on any account in an amount greater than 2 percent of that member insurer's net direct written premiums for the preceding calendar year on the kinds of insurance in the account. If the maximum assessment, together with the other assets of the Corporation in any account, does not provide in any one year in any account an amount sufficient to make all necessary payments from that account, the funds available shall be prorated and the unpaid portion shall be paid as soon thereafter as funds become available. The Corporation may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer if they are chargeable to the account for which the assessment is made.

(4) Investigate claims brought against the Corporation and adjust, compromise, settle, and pay covered claims to the extent of the Corporation's obligation and deny all

other claims and may review settlements, releases and judgments to which the insolvent insurer or its insureds were parties to determine the extent to which such settlements, releases and judgments may be properly contested.

(5) Notify such persons as the Commissioner directs under § 510(b)(1) of this subtitle.

(6) Handle claims through its employees or through one or more insurers or other persons designated as servicing facilities. Designation of a servicing facility is subject to the approval of the Commissioner, but such designation may be declined by a member insurer.

(7) Reimburse each servicing facility for obligations of the Corporation paid by the facility and for expenses incurred by the facility while handling claims on behalf of the Corporation and shall pay the other expenses of the Corporation authorized by this subtitle.

(b) The Corporation may:

(1) Employ or retain such persons as are necessary to handle claims and perform other duties of the Corporation.

(2) Borrow funds necessary to effect the purposes of this subtitle in accord with the plan of operation.

(3) Sue or be sued.

(4) Negotiate and become a party to such contracts as are necessary to carry out the purpose of this subtitle.

(5) Perform such other acts as are necessary or proper to effectuate the purpose of this subtitle.

(6) Refund to the member insurers in proportion of the contribution of each member insurer to that account that amount by which the assets of the account exceed the liabilities if, at the end of any calendar year, the board of directors finds that the assets of the Corporation in

any account exceed the liabilities of that account as estimated by the board of directors for the coming year.

§ 509. Plan of operation.

(a) *Submission of plan and amendments; when effective; effect of failure to submit plan or suitable amendments.*—(1) The Corporation shall submit to the Commissioner a plan of operation and any amendments thereto necessary or suitable to assure the fair, reasonable, and equitable administration of the Corporation. The plan of operation and any amendments thereto shall become effective upon approval in writing by the Commissioner.

(2) If the Corporation fails to submit a suitable plan of operation within 90 days following July 1, 1971, or if at any time thereafter the Corporation fails to submit suitable amendment to the plan, the Commissioner shall, after notice and hearing adopt and promulgate such reasonable rules as are necessary or advisable to effectuate the provisions of this subtitle. Such rules shall continue in force until modified by the Commissioner or superseded by a plan submitted by the Corporation and approved by the Commissioner.

(b) *Compliance by member insurers.*—All member insurers shall comply with the plan of operation.

(c) *Contents of plan.*—The plan of operation shall:

(1) Establish the procedures whereby all the powers and duties of the Corporation under § 508 will be performed.

(2) Establish procedures for handling assets of the Corporation.

(3) Establish the amount and method of reimbursing members of the board of directors under § 507.

(4) Establish procedures by which claims may be filed with the Corporation and establish acceptable forms of proof of covered claims. Notice of claims to the receiver

or liquidator of the insolvent insurer shall be deemed notice to the Corporation or its agent and a list of such claims shall be periodically submitted to the Corporation by the receiver or liquidator.

(5) Establish regular places and times for meetings of the board of directors.

(6) Establish procedures for records to be kept in all financial transactions of the Corporation, its agents, and the board of directors.

(7) Provide that any member insurer aggrieved by any final action or decision of the Corporation may appeal to the Commissioner within 30 days after the action or decision.

(8) Contain additional provisions necessary or proper for the execution of the powers and duties of the Corporation.

(d) *Delegation of powers and duties of Corporation.*—The plan of operation may provide that any or all powers and duties of the Corporation except those under §§ 508 (a)(3) and 508 (b)(2), are delegated to a corporation, association, or other organization which performs or will perform functions similar to those of this Corporation, or its equivalent. Such a corporation, association or organization shall be reimbursed as a servicing facility would be reimbursed and shall be paid for its performance of the functions of the Corporation. A delegation under this subsection shall take effect only with the approval of both the board of directors and the Commissioner, and may be made only to a corporation, association, or organization which extends protection not substantially less favorable and effective than that provided by this subtitle.

§ 510. Duties and powers of Commissioner generally; review of actions or orders.

(a) The Commissioner shall:

(1) Notify the Corporation of the existence of an insolvent insurer not later than 3 days after he received notice of the determination of the insolvency.

(2) Upon request of the board of directors, provide the Corporation with a statement of the net direct written premiums of each member insurer.

(b) The Commissioner may:

(1) Require that the Corporation notify the insureds or the principal and specific obligees named in surety bonds, of the insolvent insurer and any other known interested parties of the determination of insolvency and of their rights under this subtitle. Such notifications may be by mail at their last-known address, where available, but if sufficient information for notification by mail is not available, notice by publication in a newspaper of general circulation shall be sufficient.

(2) Suspend or revoke, after notice and hearing, the certificate of authority to transact insurance in this State of any member insurer which fails to pay an assessment when due or fails to comply with the plan of operation. As an alternative, the Commissioner may levy a fine on any member insurer which fails to pay an assessment when due. Such fine shall not exceed 5% of the unpaid assessment per month, except that no fine shall be less than $100 per month.

(3) Revoke the designation of any servicing facility if he finds claims are being handled unsatisfactorily.

(c) Any final action or order of the Commissioner under this subtitle shall be subject to judicial review in a court of competent jurisdiction.

§ 511. Effect of payment of claim; statements to be filed with receiver or liquidator of insolvent insurer.

(a) *Assignment of rights; cooperation by insured or claimant; cause of action against insured; insolvent insurer operating on plan with assessment liability.*—Any person recovering under this subtitle shall be deemed to have

assigned his rights under the policy to the Corporation to the extent of his recovery from the Corporation. Every insured or claimant seeking the protection of this subtitle shall cooperate with the Corporation to the same extent as such person would have been required to cooperate with the insolvent insurer. The Corporation shall have no cause of action against the insured of the insolvent insurer for any sums it has paid out except such causes of action as the insolvent insurer would have had if such sums had been paid by the insolvent insurer. In the case of an insolvent insurer operating on a plan with assessment liability, payments of claims of the Corporation shall not operate to reduce the liability of insureds to the receiver, liquidator, or statutory successor for unpaid assessments.

(b) *Receiver, etc., of insolvent insurer bound by settlements of covered claims; priority of claims and expenses in handling claims.*—The receiver, liquidator, or statutory successor of an insolvent insurer shall be bound by settlements of covered claims by the Corporation or its representatives. The court having jurisdiction shall grant such claims priority equal to that which the claimant would have been entitled in the absence of this subtitle against the assets of the insolvent insurer. The expenses of the Corporation or similar organization in handling claims shall be accorded the same priority as the liquidator's expenses.

(c) *Statements to be filed with receiver or liquidator of insolvent insurer.*—The Corporation shall periodically file with the receiver or liquidator of the insolvent insurer statements of the covered claims paid by the Corporation and estimates of anticipated claims on the Corporation which shall preserve the rights of the Corporation against the assets of the insolvent insurer.

§ 512. Exhaustion of rights and effect of recovery under certain policies; claims recoverable from more than one corporation.

(a) Any person having a covered claim against an insurer, including surety, under any provision in an insurance policy or surety bond, other than a policy of an insolvent insurer which is also a covered claim, shall be required to exhaust first his right under such policy or bond. Any amount payable on a covered claim under this subtitle shall be reduced by the amount of any recovery under such insurance policy or surety bond.

(b) Any person having a claim which may be recovered under more than one insurance guaranty association or its equivalent shall seek recovery first:

(1) Except with respect to a surety bond, from the Corporation of the place of residence of the insured except that if it is a first party claim for damage to property with a permanent location, he shall seek recovery first from the Corporation of the location of the property;

(2) With respect to a surety bond, from the Corporation of the place of performance of the obligation described in the bond.

(c) Any recovery under this subtitle shall be reduced by the amount of recovery from any other insurance guaranty association or its equivalent.

§ 513. Detection and prevention of insolvencies.

Repealed by Acts 1986, ch. 161, § 1, effective July 1, 1986.

§ 514. Examination and regulation by Commissioner; financial report.

The Corporation shall be subject to examination and regulation by the Commissioner. The board of directors shall submit, not later than March 30 of each year, a

financial report for the preceding calendar year in a form approved by the Commissioner.

§ 515. Exemption from payment of fees and taxes.

The Corporation shall be exempt from payment of all fees and all taxes levied by this State or any of its subdivisions except taxes levied on real or personal property.

§ 516. Recoupment of assessments paid by member insurers.

The rates and premiums charged for insurance policies and surety bonds to which this subtitle applies shall include amounts sufficient to recoup over a reasonable length of time which shall not be less than three years, a sum equal to the amounts paid to the Corporation by the member insurer less any amounts returned to the member insurer by the Corporation and such rates shall not be deemed excessive because they contain an amount reasonably calculated to recoup assessments paid by the member insurer.

§ 517. Immunity from liability.

There shall be no liability on the part of and no cause of action of any nature shall arise against any member insurer, the Corporation or its agents or employees, the board of directors, or the Commissioner or his representatives for any action taken by them in the performance of their powers and duties under this subtitle. Notwithstanding the provisions of this section, the Corporation is not and may not be deemed a department, unit, agency, or instrumentality of the State.

§ 518. Stay of proceedings involving insolvent insurers; setting aside default judgment, etc.

All proceedings in which the insolvent insurer is a party or is obligated to defend a party in any court in this State shall be stayed for 60 days from the date the insolvency is determined to permit proper defense by the Corporation of all pending causes of action. As to any covered claims

arising from a judgment under any decision, verdict or finding based on the default of the insolvent insurer or its failure to defend an insured, the Corporation either on its own behalf or on behalf of such insured may apply to have such judgment, order, decision, verdict or finding set aside by the same court or administrator that made such judgment, order, decision, verdict or finding and shall be permitted to defend against such claim on the merits.

§ 519. Termination; distribution of moneys and assets; expiration of subtitle.

(a) *Termination as to certain kind of insurance—In general.*—The Commissioner shall by order terminate the operation of the Property and Casualty Insurance Guaranty Corporation as to any kind of insurance covered by this subtitle with respect to which he has found, after hearing, that there is in effect a statutory or voluntary plan which:

(1) Is a permanent plan which is adequately funded or for which adequate funding is provided; and

(2) Extends, or will extend to the Maryland policyholders and residents protection and benefits with respect to insolvent insurers not substantially less favorable and effective to such policyholders and residents than the protection and benefits provided with respect to such kinds of insurance under this subtitle.

(b) *Same—Discontinuance of future payments by insurers.*—The Commissioner shall by the same order authorize discontinuance of future payments by insurers to the Corporation with respect to the same kinds of insurance; provided, the assessments and payments shall continue, as necessary, to liquidate covered claims of insurers adjudged insolvent prior to said order and the related expenses not covered by such other plan.

(c) *Termination as to all kinds of insurance; distribution of moneys and assets; expiration of subtitle.*—In the event the operation of the Property and Casualty Insurance

Guaranty Corporation shall be so terminated as to all kinds of insurance otherwise within its scope, the Corporation as soon as possible thereafter shall distribute the balance of moneys and assets remaining (after discharge of the functions of the Corporation with respect to prior insurer insolvencies not covered by such other plan, together with related expenses) to the insurers which are then writing in this State policies of the kinds of insurance covered by this subtitle and which had made payments to the Corporation, pro rata upon the basis of the aggregate of such payments made by the respective insurers during the period of five years next preceding the date of such order. Upon completion of such distribution with respect to all of the kinds of insurance covered by this subtitle, this subtitle shall be deemed to have expired.

Supreme Court, U.S.
FILED
OCT · 21 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-302

In the Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, PETITIONER

v.

UNITED STATES DEPARTMENT OF THE TREASURY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether a Maryland statute establishing the priority of various classes of claims against the assets of an insolvent insurance company, Md. Code Ann. art. 48A, §§ 158, 158A (1957), regulates the "business of insurance" within the meaning of Section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. 1012(b), so as to avoid the priority conferred by 31 U.S.C. 3713 on claims by the United States.

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In the Supreme Court of the United States

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UNITED STATES DEPARTMENT OF THE TREASURY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-5a) is reported at 846 F.2d 272. The opinion of the district court (Pet. App. 6a-22a) is reported at 668 F. Supp. 483.

JURISDICTION

The judgment of the court of appeals was entered on May 20, 1988. The petition for a writ of certiorari was filed on August 18, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner, a Special Deputy Insurance Commissioner of Maryland, is the receiver of an insolvent insurer, the Eastern Indemnity Insurance Company (EICOM).

EICOM was licensed to do business in Maryland in 1980 and eventually operated in 30 states (Pet. App. 7a). Its principal business was the underwriting of surety bonds for contractors (*ibid.*). In 1985, the Circuit Court for Montgomery County, Maryland, ordered EICOM's liquidation, and it was declared insolvent (*ibid.*). Petitioner was appointed to wind up EICOM's affairs in accordance with the Maryland Insurance Code (*ibid.*). That statute establishes a comprehensive scheme for administering the liquidation of insolvent insurance companies (*id.* at 9a). In particular, it defines the types of claims which may be filed against an insurance company undergoing liquidation, and creates priorities for payment of those claims (*id.* at 9a-10a). See Md. Ann. Code art. 48A, §§ 158, 158A (1957). In this case, the assets of EICOM are far less than would be necessary to satisfy all claimants in full (Pet. App. 7a).

In the liquidation proceeding, the Treasury Department made claims based on performance and payment bonds issued by EICOM in connection with various Miller Act construction projects (Pet. App. 8a). Under the terms of the Maryland statute, these claims would fall within the fourth priority, *i.e.*, "[c]laims by policyholders, beneficiaries, and insureds * * * " (Md. Ann. Code art. 48A, § 158A (1957); see Pet. App. 10a, 44a). The government, however, asserted an absolute priority for its claims under 31 U.S.C. 3713(a). This statute (Pet. App. 24a-25a) requires that a claim of the United States government be "paid first" when an insolvent debtor performs an act of bankruptcy or insolvency.[1]

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[1] Section 3713 does not apply to cases under the federal bankruptcy statute. Insurance companies are excluded from that statute. 11 U.S.C. 109(b).

2. Petitioner contested the government's claim by filing suit in the United States District Court for the District of Maryland. The complaint sought a declaratory judgment that the priority asserted by the government violated Section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. 1012(b), which provides that no federal statute "shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance * * * " (see Pet. App. 23a). The district court found that the Maryland liquidation statute is intended to regulate the insurance industry and that enforcement of Section 3713 would invalidate, impair, or supersede the state statute (Pet. App. 12a). However, it held that the McCarran-Ferguson Act does not foreclose the priority Section 3713 confers on the United States because "the liquidation of an insolvent insurance company and the priority of claims paid thereto does not constitute the 'business of insurance' as that term is used in" the Act (Pet. App. 21a).

The district court reached this conclusion after reviewing at length the cases in which this Court has determined whether various activities regulated by state law constitute the "business of insurance" for purposes of the Act (Pet. App. 12a-17a). It determined that the three criteria set forth in *Group Life & Health Ins. Co.* v. *Royal Drug Co.*, 440 U.S. 205 (1979), and *Union Labor Life Ins. Co.* v. *Pireno*, 458 U.S. 119 (1982), are "absolutely controlling" (Pet. App. 17a) on the question whether a practice regulated by state law is part of the "business of insurance." These criteria are: first, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within

the insurance industry (*id.* at 15a). See *Pireno*, 458 U.S. at 129.

The district court found that the liquidation statute at issue in this case satisfies none of these criteria. With respect to the first, it explained that the risk that an insurance company will become insolvent is not the kind of risk whose transfer was referred to in *Pireno* and *Royal Drug*. "The obligation of EICOM under its insurance policies to insure against risks of loss is wholly different from the procedure an insurance company must follow to pay claimants in case of insolvency" (Pet. App. 18a). The court also found that the Maryland insolvency scheme is not, in terms of the second prong of the *Pireno* test, "an 'integral part' of the relationship between the insured and the insurer" (*id.* at 20a). The district court explained that "[t]he contractual liability to pay on a policy of insurance is obviously distinct from the question of who gets paid first" (*ibid.*). Finally, with respect to the last of the *Pireno* criteria, the court found that the "liquidation of EICOM and the payment of claims involve entities outside the insurance industry" (*id.* at 21a).

3. The court of appeals affirmed the district court's decision in a brief per curiam opinion (Pet. App. 1a-5a). It rejected petitioner's contention that the district court had erred in relying on *Pireno* and *Royal Drug* "outside of the antitrust context" (*id.* at 4a). The court of appeals also approved the district court's analysis of the three factors set out in those cases, except that it found it unnecessary to decide whether the district court had correctly characterized the first factor as "indispensable" (*id.* at 4a-5a). In all other respects, it adopted the district court's opinion as its own (*id.* at 5a).

ARGUMENT

1. Since the filing of the petition, the Ninth Circuit has joined the Fourth Circuit in holding that state statutes establishing the priority of claims against an insolvent insurance company do not regulate the "business of insurance" within the meaning of the McCarran-Ferguson Act. See *Idaho ex rel. Soward* v. *United States,* No. 87-4057 (9th Cir. Sept. 7, 1988). In *Idaho,* the Internal Revenue Service asserted priority under Section 3713 for its claims for unpaid federal taxes against two insolvent insurance companies. The Director of Idaho's Department of Insurance, who had taken possession of the companies' assets, argued that they should instead be distributed in accordance with the Idaho Insurers' Supervision, Rehabilitation and Liquidation Act, Idaho Code §§ 41-3301 to 41-3360 (1977 & Supp. 1988), and that Section 2(b) of the McCarran-Ferguson Act made the priority established by Section 3713 inapplicable. The Ninth Circuit, reversing a decision by the district court,[2] held that the United States was entitled to priority. It found that this Court's decision in *Securities & Exchange Comm'n* v. *National Securities, Inc.,* 393 U.S. 453 (1969), compelled the conclusion that Idaho's priority statute "is *not* a law regulating the business of insurance" (slip op. 12544 (emphasis in original)). The Ninth Circuit explained (*ibid.*):

> To begin with, the statute deals with insurance companies that no longer are in the business of insurance. The only "business" being conducted is the liquidation of a corporation which happens to have been an

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[2] *Idaho ex rel. Soward* v. *United States,* 662 F. Supp. 60 (D. Idaho 1987). As a result of the reversal, which postdated the filing of the petition, petitioners can no longer rely on the district court's decision as a basis for urging further review. See Pet. 17-18.

> insurance company. Hence, the scope of the net cast by the statute is wholly unrelated to the relationship between insurer and insured. The insurer has ceased to exist. The only relationship is between the insureds and the government official charged with overseeing the liquidation of the insolvents. * * * The relationship regulated by [the liquidation statute] that is at issue in this case is between the liquidated assets of corporations and the claims of various creditors.

On a "second level of analysis," the Ninth Circuit also joined the court of appeals in this case in concluding that the three criteria set out in *Royal Drug* and *Pireno* require the conclusion that this type of statute does not regulate the "business of insurance" (*Idaho,* slip op. 12545-12549).[3]

Contrary to the suggestion of amicus Superintendent of Insurance of the State of New York (James P. Corcoran Amicus Br. 5-7), these holdings of the Fourth and Ninth Circuits are not inconsistent with any decision of the Second Circuit. In *Levy* v. *Lewis,* 635 F.2d 960 (2d Cir. 1980), and *Law Enforcement Ins. Co.* v. *Corcoran,* 807 F.2d 38 (2d Cir. 1986) cert. denied, 481 U.S. 1017 (1987), the Second Circuit held only that it was appropriate for federal courts to abstain from adjudicating claims against insolv-

[3] The only state court decision to address this issue of which we are aware reached the same result. *Langdeau* v. *United States,* 363 S.W.2d 327 (Tex. Ct. Civ. App. 1962). *Langdeau* rejected the contention that a state statute establishing the priority of claims for unpaid wages against an insolvent insurance company is "a regulation of the insurance business" within the meaning of the McCarran-Ferguson Act (*id.* at 331). Instead, the court said, "it is a priority established for a class of creditors of an insurance company. There are many statutes regulating the rights of persons who may have claims against an insurance company * * *, yet it would hardly be contended that these laws regulate the insurance business simply because they may be invoked against an insurance company" (*ibid.*). The court held, accordingly, that the United States had priority under the predecessor of Section 3713 for its claims for unpaid taxes and interest on them.

ent insurers where a state regulatory scheme committed such claims to a single state court. While the Second Circuit invoked the underlying policy of the McCarran-Ferguson Act and the existence of detailed state regulation of insolvent insurers as factors weighing in favor of abstention,[4] it did not hold that an insurer liquidation statute regulated the "business of insurance" so as to displace inconsistent federal law. To the contrary, in *Levy* the court made it unmistakably clear that the McCarran-Ferguson Act would not preclude the application of federal law (ERISA) to the merits of a claim against an insurer in liquidation, "since the Act was meant only to free state regulation 'of the business of insurance' [quoting *National Securities,* 393 U.S. at 459-460], not regulation of insurers as employers * * *." 635 F.2d at 966. In short, there is no disagreement among the courts of appeals on the issue presented by this case.

2. Nor is there any conflict between the Fourth Circuit's ruling in this case and decisions of this Court. As both the Fourth and Ninth Circuits have now held, a state statute establishing priorities among classes of claims against an insolvent insurer does not, under the three-part test set out in *Pireno* and *Royal Drug,* regulate "the business of insurance." That conclusion is inescapable. Once an insurance company is in liquidation, it is no longer in the business of insurance. While the insurer's assets must be distributed among various creditors, some of which are policyholders with claims based on their policies, a statute establishing the order of payment has nothing to do with the manner in which the policy trans-

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[4] *Levy*, 635 F.2d at 960 (characterizing as "highly significant" the fact that "the state scheme has been adopted pursuant to congressional authorization," *i.e.,* the McCarran-Ferguson Act, and describing the Act as embodying an "express federal policy of noninterference in insurance matters"); *Law Enforcement Ins. Co.*, 807 F.2d at 44 (quoting *Levy*).

fers risk, is not an integral part of the relationship between insured and insurer, and applies not only to entities within the insurance industry (whether insured or insurer) but also to various creditors that have transacted business with the insurer.

Apparently acknowledging the force of the lower courts' application of the *Pireno* criteria, petitioner's principal argument is that those criteria should not apply to this case (Pet. 14-16). Invoking this Court's discussion in *Royal Drug* of the "primary" and "secondary" purposes of the McCarran-Ferguson Act, he contends that *Pireno*'s analysis was meant only to govern the availability of an exemption from the federal antitrust laws (Pet. 12, 14-17). This argument cannot be reconciled with the language of the Act and misapprehends *Royal Drug*'s description of its purposes.

Both *Pireno* and *Royal Drug,* like this case, applied Section 2(b) of the Act. By its terms, this Section resolves any conflict between an "Act of Congress" that does not "specifically relate[ ] to the business of insurance" and a state law "enacted * * * for the purpose of regulating the business of insurance." In this regard, Section 2(b) does not distinguish between antitrust statutes and other Acts of Congress, and thus permits no difference in the meaning of the phrase "business of insurance" depending on what federal statute is involved. If a state law regulates the "business of insurance," it supersedes all inconsistent general federal statutes; if it does not, it is subordinate to all such federal laws.

Royal Drug's description of the two "purposes" of the Act does not suggest a different conclusion. The "primary purpose" of the Act is, as this Court made clear there, "to preserve state regulation of the activities of insurance companies as it existed before the *South-Eastern Underwriters* case [322 U.S. 533 (1944)]," that is, to permit the States to

continue such regulation "without fear of Commerce Clause attack" (*Royal Drug*, 440 U.S. at 218 n.18).[5] This purpose is expressed in Section 1 of the Act, which declares state regulation of the business of insurance to be in the public interest, and is implemented in Section 2(a), which authorizes state regulation of "the business of insurance, and every person engaged therein." [6] This purpose is not implicated in this case, since no one is suggesting that the Commerce Clause precludes any State from enacting a statute of the type in issue here. The "secondary" purpose of the Act, which is embodied in Section 2(b), is to reverse the result that the Supremacy Clause would require when a state law regulating the "business of insurance" comes into conflict with a general federal statute.[7] Though this Court described that purpose in

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[5] *United States* v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), held that interstate insurance transactions constitute "Commerce among the several States" and are thus subject to Congress's power to enact legislation under the Commerce Clause. The decision led to concern, which in retrospect seems overstated, that extensive state regulation of insurance companies would be invalidated by negative implication of the Commerce Clause. See *Prudential Ins. Co.* v. *Benjamin*, 328 U.S. 408 (1946).

[6] In this respect, Section 2(a) is broader than Section 2(b). Congress has delegated power to the States to regulate not only "the business of insurance" but also "every person engaged therein." However, such state laws are supreme only if they fall into the first of these categories—*i.e.*, if they regulate "the business of insurance." This distinction between the States' power to regulate and the exemption of their laws from inconsistent general federal statutes evokes this Court's oft-quoted statement that Section 2(b) applies to "the 'business of insurance,' not the 'business of insurers.' " *Royal Drug*, 440 U.S. at 211.

[7] Congress's immediate concern, of course, was that unforeseen conflicts would occur through interpretation of federal statutes in light of *South-Eastern Underwriters'* novel recognition of the breadth of Congress's power to regulate insurance under the Commerce

terms of the antitrust laws in *Royal Drug* (440 U.S. at 218-219), since that was the type of statute involved there, nothing in the Act or its legislative history limits that purpose to any particular kind of federal law. In fact, in *Securities & Exchange Comm'n* v. *National Securities, Inc., supra,* the seminal decision on the meaning of the phrase "business of insurance" for purposes of Section 2(b), the federal statute involved was one of the Securities Acts, and not an antitrust law. Accordingly, application in non-antitrust cases of the three factors in terms of which this Court has further specified "the business of insurance" does not contradict any of the Act's purposes.

Use of the three *Pireno* criteria also does not conflict with the reasoning or results in *Robertson* v. *California,* 328 U.S. 440 (1946), and *Federal Trade Comm'n* v. *National Casualty Co.,* 357 U.S. 560 (1958). See Pet. 15-17. In *Robertson,* a case involving a criminal conviction for a violation of a state insurance statute which had occurred before the McCarran-Ferguson Act's passage, the Court expressly "refrained from explicit reliance upon the Act" in order "to avoid any semblance of retroactive effect in a criminal matter" (328 U.S. at 462). The Court's holdings that the state statute was not invalid under the Commerce Clause and other constitutional provisions did not address any conflict between state and federal statutes and are thus irrelevant to this case. Similarly, the Court's very brief per curiam decision in the *National Casualty* case did not specifically discuss the scope of Section 2(b)'s exemption

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Clause. By contrast, there had never been doubt about the comprehensiveness of Congress's power under Article I, Section 8 of the Constitution to establish "uniform Laws on the subject of Bankruptcies throughout the United States * * *." The statutory term "business of insurance" is properly interpreted in light of these background considerations, as this Court's rationale in the *National Securities* case makes clear (see pages 11-12, *infra*).

for the "business of insurance." In any event, since the activity in issue there, insurer advertising, was closely related to the sale of insurance policies to policyholders, it would have been entirely plausible to find, contrary to petitioner's suggestion (Pet. 16), that those activities were related to the transfer of the policyholder's risk, were a part of the relationship between the insurer and insured, and were limited to entities, *i.e.*, insurers, their agents and potential customers, that are part of the insurance industry.

3. Petitioner and some of the amici suggest that Section 2(b) should be extended to all aspects of "cradle to grave" regulation of insurance companies. Pet. 22; State of Maryland Amicus Br. 5-9; James P. Corcoran Amicus Br. 4-5. However, as the Ninth Circuit correctly recognized, this contention begs the question of whether the specific provision at issue in this case constitutes "the type of regulation that Congress sought to protect from indirect federal preemption by passing the McCarran-Ferguson Act." *Idaho*, slip op. 12549. The unmistakable thrust of this Court's cases is to require a showing that the particular state provision in issue regulates the "business of insurance." It has never been sufficient to show that such a provision is included in a regulatory scheme some parts of which satisfy that test. Petitioner's broad view of the McCarran-Ferguson Act would also run against its legislative history. As this Court explained in *National Securities, Inc.*, 393 U.S. at 458-459:

> The McCarran-Ferguson Act was an attempt to turn back the clock, to assure that the activities of insurance companies in dealing with their policyholders would remain subject to state regulation. As the House Report makes clear, "[i]t [was] not the intention of Congress in the enactment of this legislation to

> clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association* case." H.R. Rep. No. 143, 79th Cong., 1st Sess., 3 (1945).

While not dispositive of the issues in this case, this history suggests that Section 2(b) cannot be viewed as a complete exemption for all state "cradle to grave" insurance regulation. As we have explained (note 7, *supra*), Congress's power to establish uniform bankruptcy laws is expressly conferred by Article I of the Constitution and hence long antedates the *Southeastern Underwriters* decision.

4. The persistent undertone of the petition and the briefs filed by the amici is that it is unfair for the United States to obtain priority over other policyholders when an insurance company becomes insolvent. See, *e.g.*, Pet. 6-7, 18-20; Property and Casualty Insurance Guaranty Corporation, et al. Amicus Br. 13-16. However, the scope of the "business of insurance" for purposes of the McCarran-Ferguson Act does not depend on value judgments concerning the relative virtues of conflicting state and federal statutes in a particular case. Moreover, if petitioner's position were adopted, the result would not just abrogate the United States' priority as a policyholder. It would also require the claims of private parties claiming under federal statutes and other types of federal government claims to be subordinated in accordance with whatever scheme of priorities a State might choose to establish. See *Langdeau* v. *United States,* 363 S.W.2d at 331 ("If the preference given by [the state statute] is to prevail over the tax claim of the government, then a State may not only prefer employees of the company, but may prefer every other

claim and make the debt due the United States last. We find nothing in the McCarran Act to warrant this result.").[8] The particular character of the claims at issue in this case does not make it more worthy of this Court's review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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[8] The statute giving the United States priority, 31 U.S.C. 3713, has been in effect since virtually the beginning of the Republic (see Act of Mar. 3, 1797, ch. 20, § 5, 1 Stat. 515, as amended by Act of Mar. 2, 1799, ch. 22, § 65, 1 Stat. 676, and advances the public policy of securing adequate revenue to sustain the public burden and discharge the public debts. *United States* v. *State Bank of North Carolina*, 31 U.S. (6 Pet.) 29, 35 (1832).

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Respondents.

REPLY TO RESPONDENTS' BRIEF IN OPPOSITION

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Petitioner James A. Gordon, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland, respectfully submits this Reply to Respondents' Brief in Opposition. In accordance with Rule 22.5 of this Court, this Reply addresses only those arguments first raised by Respondents in their Brief in Opposition.[1]

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[1] This Reply does not, as a result of Rule 22.5, address the fundamental misunderstanding of the text, purpose and legis-

Respondents argue (incorrectly, we submit) that the instant Petition should not be granted because in *Idaho ex rel. Soward v. United States*, No. 87-4057, (9th Cir. Sept. 7, 1988), decided nearly three weeks after the Petition was filed, the United States Court of Appeals for the Ninth Circuit reached the same result as did the court below in a case presenting substantially the same question as is presented here. Respondents' Brief at 5-7. In fact, that case highlights the confusing judicial positions which must be resolved by this Court and counsels in favor of granting the Petition.

In *Soward*, the Ninth Circuit explicitly rejected the analysis adopted by the United States Court of Appeals for the Fourth Circuit below, and held that the analysis of this Court in *Securities and Exchange Comm'n v. National Securities, Inc.*, 393 U.S. 453 (1969) is the proper vehicle for interpreting the term "business of insurance" in cases arising under the primary regulatory purpose of the McCarran-Ferguson Act. Under the *National Securities* test, as employed by the Ninth Circuit, the focus is on "the relationship between the insurance company and the policyholder." *Id.* at 460. Significantly, the Ninth Circuit explicitly held that the test announced in *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979) and *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982) is inapplicable to a case arising under the McCarran-Ferguson Act's primary state

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lative history of the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, demonstrated by Respondents' Brief. Instead, Petitioner relies upon the analysis more fully developed at 10-18 of his Petition for an explanation of the invalidity of Respondents' arguments.

regulatory purpose.[2] The Ninth Circuit correctly recognized that because the *Royal Drug-Pireno* test is "tailored to address activities of insurance companies that would implicate the *antitrust laws* in the absence of the McCarran-Ferguson Act" (emphasis supplied), it is inapplicable to a case such as the one at bar.

The totally different approaches used by the Ninth and Fourth Circuits to resolve nearly identical questions exacerbates the already pervasive confusion surrounding what is meant by the "business of insurance" in the context of the McCarran-Ferguson Act's primary state regulatory purpose. A serious conflict, therefore, exists between the circuits. Significantly, many state statutes which the Ninth Circuit would hold regulate the business of insurance under the *National Securities* analysis, would be found to not regulate the business of insurance under the Fourth Circuit's *Royal Drug-Pireno* analysis.

For example, state insurance laws requiring that insurers make prompt payment after a covered loss and engage in good faith claims settlement practices[3] regulate the business of insurance under the Ninth Circuit's *National Securities* analysis because they directly involve the relationship between the insurer and the policyholder. However, such statutes do not regulate the business of insurance under the Fourth

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[2] Although the Ninth Circuit also employed the three-part *Royal Drug-Pireno* test as further support for its holding, that analysis was dicta and the court explicitly stated that the *Royal Drug-Pireno* test was not applicable. "*National Securities* and the legislative history alone are enough to decide this case without the three prongs of *Royal Drug*."

[3] *See, e.g.*, Md. Code art. 48A, § 230A; Va. Code § 38.2-510.

Circuit's *Royal Drug-Pireno* analysis because these same laws are unrelated to the underwriting or spreading of risk. This is because, according to the Fourth Circuit's *Royal Drug-Pireno* test, whether the policyholder's claim is ultimately paid upon the occurrence of a covered loss is irrelevant to the definition of "business of insurance" because the risk of loss is fully transferred once the policy is issued and the ultimate payment of a claim is "temporally unconnected" to the transfer of risk. Pet. App. at 18a-20a.

Furthermore, contrary to Respondents' suggestion, the Fourth Circuit's analysis directly conflicts with the result reached by this Court in *Federal Trade Comm'n v. National Casualty Co.*, 357 U.S. 560 (1958). Because insurer advertising is completely unrelated to the underwriting of policyholder risk, *National Casualty* would have to be decided differently under the Fourth Circuit's analysis. Significantly, *National Casualty* would be decided as it originally was under the Ninth Circuit's analysis because laws barring false or misleading advertising by insurance companies do involve the relationship between the insurer and the policyholder, and would therefore constitute the "business of insurance" for purposes of the McCarran-Ferguson Act.

More importantly, Respondents err in arguing that the statutes at issue in *National Casualty* regulated the business of insurance because advertising is "closely related" to the sale of insurance policies and, therefore, relate to the underwriting or spreading of risk, whereas, according to Respondents, the Mary-

land priority of payment statutes do not regulate the business of insurance. In fact, the Maryland statutes at issue bear a far stronger relationship to the transfer of policyholder risk because they ensure that policyholders are paid to the fullest extent possible. Accordingly, the Fourth Circuit's use of the *Royal Drug-Pireno* test in this context is in direct conflict with this Court's holding in *National Casualty*.

Additionally, contrary to Respondents' suggestion, the opinion of the Fourth Circuit also conflicts with the rationale underlying two Second Circuit opinions addressing insurance company insolvency proceedings. The broad language of the Fourth Circuit's holding that the Maryland priority of payment statutes do not regulate the business of insurance necessarily means that the policies of the McCarran-Ferguson Act simply do not apply to those statutes. This is inconsistent with *Levy v. Lewis*, 635 F.2d 960 (2d Cir. 1980) and *Law Enforcement Ins. Co. v. Corcoran*, 807 F.2d 38 (2d Cir. 1986), *cert. denied*, 481 U.S. 1017 (1987), which recognized that the McCarran-Ferguson Act's deferral to state regulation extends to the regulation of insurer insolvency.[4] The sweeping nature of the

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[4] Although the opinions in Levy and Corcoran dealt with the narrow issue of whether federal courts should abstain from exercising federal jurisdiction in federal actions involving insurance companies in liquidation, the analysis of these opinions makes clear that state regulation of insolvent insurance companies is part and parcel of the state's regulation of insurance, as to which there exists an express federal policy of non-interference. Levy, 635 F.2d at 963. Moreover, if, as suggested by Respondents, insurance company insolvencies do not involve the "business of insurance" because the company is no longer involved in the "business of insurance" once it loses its financial viability (Respondents' Brief at 7), the express exclusion by Congress of

Fourth Circuit's holding that the McCarran-Ferguson Act does not apply to insurer insolvency casts serious doubt on the continued primacy, if not future viability of state regulation of insurer insolvency.

All of the foregoing demonstrates the importance of the instant Petition. It is even more apparent now that the Ninth Circuit has spoken that there exists serious conflict among the circuits and between the decisions of this Court regarding the definition of the business of insurance in the context of the primary purpose of the McCarran-Ferguson Act. The confusion and likely potential for inconsistent results extends far beyond the confines of this litigation, as future cases arising under identical fact patterns will be decided differently, depending upon which decision is followed. Only this Court can clear up this confusion and authoritatively announce the test for the business of insurance in cases arising under the primary state regulatory purpose provisions of the McCarran-Ferguson Act.

Significantly, Respondents never quarrel with the fact that the issues at bar are of singular national importance and require prompt resolution. Indeed, Respondents' Brief is entirely silent on the point. As demonstrated by the *amicus* brief of the National Association of Insurance Commissioners, many insurance company insolvencies involving the claims of numerous policyholders are pending. The conflicting opinions of the Fourth and Ninth Circuits have cast a cloud of confusion upon these proceedings. There is, therefore, a compelling need for this Court to act in this area.

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insurance company insolvencies from the bankruptcy code makes no sense. 11 U.S.C. § 109(b)(2, 3).

CONCLUSION

For all of the foregoing reasons, the Petition for Certiorari should be granted.

Respectfully submitted,

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SUPPLEMENTAL BRIEF OF PETITIONER

Petitioner James A. Gordon, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland, respectfully submits this Supplemental Brief. In accordance with Rule 22.6, this Supplemental Brief brings to this Court's attention two recent cases, as yet unavailable in the advance sheets, which further demonstrate that this Court must act to clarify the confusion which exists within the circuits regarding the primary state regulatory purpose provisions of the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*

In *Crist v. J. Henry Schroder Bank & Trust Co.*, No. 87 CIV 1845 (S.D. N.Y. Oct. 14, 1988),[1] decided three weeks ago, the United States District Court for the Southern District of New York (Knapp, J.) abstained from hearing a suit brought against an insurance company undergoing insolvency proceedings in Missouri. In so holding, the court relied upon two Second Circuit cases, *Law Enforcement Ins. Co. v. Corcoran*, 807 F.2d 38 (2d Cir. 1986), *cert. denied*, 481 U.S. 1017 (1987) and *Levy v. Lewis*, 635 F.2d 960 (2d Cir. 1980), which emphasized that the McCarran-Ferguson Act's deferral to the state regulation of insurance extends to the establishment of comprehensive state systems for liquidating insolvent insurance companies. As Petitioner demonstrated in his Reply at 5-6, the sweeping language of the Fourth Circuit opinion below is inconsistent with these Second Circuit holdings because abstention is functionally equivalent to McCarran-Ferguson Act preemption. The opinion in *Crist*, therefore, highlights the differing constructions of the primary purpose of the McCarran-Ferguson Act within the circuits and underscores both the confusion which exists with regard to this important issue and the compelling need for this Court to clarify this jurisprudence.

Similarly, less than one month before *Crist* was decided, the United States Court of Appeals for the Tenth Circuit also adopted the Second Circuit's rationale in *Levy* by holding that a district court should have abstained from hearing a federal claim against an insurance company undergoing state liquidation proceedings because the McCarran-Ferguson Act's deferral to state regulation of insurance includes state

[1] The slip opinion is available on *Westlaw* at 1988 WL 105987.

regulation of insurance insolvencies. *Grimes v. Crown Life Ins. Co.*, No. 86-1905 (10th Cir. Sep. 16, 1988).[2] As indicated, this analysis, adopted by the Second and Tenth Circuits, directly conflicts with the conclusion reached by the Fourth Circuit below and the recent opinion of the Ninth Circuit in *Idaho ex rel. Soward v. Internal Revenue Service*, No. 87-4057 (9th Cir. Sep. 7, 1988), discussed in Petitioner's Reply Brief at 2-3.

Significantly, the *Grimes* court also relied upon *United Services Automobile Ass'n v. Muir*, 792 F.2d 356 (3rd Cir. 1986), *cert. denied*, 107 S. Ct. 875 (1987) as support for its holding. A brief examination of the Third Circuit's opinion in *Muir* underscores the depth of the divisions between the circuits in interpreting the primary state regulatory purpose provisions of the McCarran-Ferguson Act.

In *Muir*, United Services Automobile Association ("USAA") challenged a Pennsylvania statute which barred insurance companies from doing business in the state if they also owned a financial institution. Accordingly, the statute at issue in *Muir* arose pursuant to the primary state regulatory provisions of the McCarran-Ferguson Act. The district court abstained from hearing USAA's suit because the McCarran-Ferguson Act gave the states exclusive control over the regulation of insurance, and properly cited *Levy* for the proposition that regulation of the business of insurance includes the liquidation of insolvent insurance companies.

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[2] The opinion will be reported at 857 F.2d 699.

The United States Court of Appeals for the Third Circuit reversed the district court decision to abstain but agreed with the lower court that regulation of an insolvent insurance company constitutes state regulation of insurance under the primary purpose provisions of the McCarran-Ferguson Act. Significantly, in reaching this conclusion, the Third Circuit employed the test announced by this Court in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129 (1982) for determining whether a particular state statute regulates the business of insurance - the very case relied upon by the Fourth Circuit below in reaching the exact opposite result. 792 F.2d at 364.[3] Although the Third Circuit held that the Pennsylvania statute which prohibited USAA from owning a bank did not regulate the business of insurance under the three-part *Pireno* test, the court squarely concluded that state laws regulating insurance insolvency do regulate the business of insurance under *Pireno*. *Id.* As the Third Circuit wrote,

> the state regulations implicated in Levy concerned both the future coverage of policyholders and their relationship with a defunct insurer, and so were authorized under McCarran-Ferguson.

Id.

The significance of this conclusion and the stark conflict between the Third, Fourth and Ninth Circuits can hardly be denied. The Fourth Circuit held below

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[3] As Petitioner argues in his Petition at 14-16, the *Pireno* test, announced in the context of the McCarran-Ferguson Act's limited antitrust exemption, is an inappropriate vehicle for deciding cases arising under the primary purpose of the statute.

that the *Pireno* test applies to cases arising under the primary state regulatory purpose provisions of the McCarran-Ferguson Act and that state statutes regulating insurance insolvencies do not regulate the business of insurance upon application of the *Pireno* test. The Third Circuit reached exactly the opposite result, concluding that state statutes regulating insurance insolvencies do regulate the business of insurance upon application of the same *Pireno* test. The Ninth Circuit has reached yet a third result, concluding that the *Pireno* test does not apply, but that state statutes regulating insurance insolvencies do regulate the business of insurance upon application of the test announced in *Securities and Exchange Comm'n v. National Securities, Inc.*, 393 U.S. 453 (1969). *See Idaho ex rel. Soward v. Internal Revenue Service*, No. 87-4057. Moreover, the Second and Tenth Circuits have reached results inconsistent and diametrically opposed to the decision below.

CONCLUSION

The fact that the various circuits have employed different analyses has significant ramifications far beyond the confines of the instant litigation. The recent decisions of the Southern District of New York and the Tenth Circuit, particularly the latter court's reliance on the Third Circuit analysis, further underscore the need for prompt resolution of the important

questions at bar. For all of the foregoing reasons, the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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No. 88-302

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*,

Respondents.

AMICI CURIAE BRIEF OF THE PROPERTY AND CASUALTY INSURANCE GUARANTY CORPORATION, THE ILLINOIS INSURANCE GUARANTY FUND, THE WISCONSIN INSURANCE SECURITY FUND AND JAMES T. ODIORNE IN HIS CAPACITY AS TEXAS ANCILLARY RECEIVER FOR EASTERN INDEMNITY COMPANY OF MARYLAND

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IN THE

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AMICI CURIAE BRIEF OF THE PROPERTY AND CASUALTY INSURANCE GUARANTY CORPORATION, THE ILLINOIS INSURANCE GUARANTY FUND, THE WISCONSIN INSURANCE SECURITY FUND AND JAMES T. ODIORNE IN HIS CAPACITY AS TEXAS ANCILLARY RECEIVER FOR EASTERN INDEMNITY COMPANY OF MARYLAND

The Amici Curiae respectfully pray that James A. Gordon's petition that a writ of certiorari issue to review the opinion of the United States Court of Appeals for the Fourth Circuit be granted.

CONSENT

Pursuant to United States Supreme Court Rule 36.1, a copy of the written consent of the Parties to the filing of this Amici Curiae Brief on behalf of The Property and

Casualty Insurance Guarantee Corporation, the Illinois Insurance Guaranty Fund, the Wisconsin Insurance Security Fund, and James T. Odiorne in his capacity as Texas Ancillary Receiver for Eastern Indemnity Company of Maryland, is separately enclosed.

STATEMENT OF THE CASE

The Petitioner asks this Court to decide a critical issue under the McCarran-Ferguson Act and to thereby resolve a conflict between:

(1) The Maryland insurer liquidation statute which requires a liquidator to pay claims of policyholders in full prior to paying other creditors' claims (MD. ANN. CODE art. 48A, § 132 *et seq.* (1986)); and

(2) A federal statute first enacted in 1797 which provides that a claim of the United States shall be paid first when a person indebted to the government is insolvent (31 U.S.C.A. § 3713 (West Supp. 1988)).

The McCarran-Ferguson Act, 15 U.S.C.A. § 1011 *et seq.* (West 1976), provides that the business of insurance shall be regulated by the states and that "[n]o Act of Congress shall be construed to invalidate, impair or supersede any [state] law . . . regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." The McCarran-Ferguson Act thus mandates that conflicts be resolved in favor of state laws regulating the "business of insurance" absent specific application of federal law to the insurance business. Nevertheless, the District Court ruled in favor of the general federal priority statute, reasoning that the Maryland statute governing insur-

ance company insolvency and liquidation proceedings was not a law enacted for the purpose of regulating the "business of insurance" as that term is defined under the McCarran-Ferguson Act. The United States Court of Appeals for the Fourth Circuit affirmed the District Court's decision, adopting the lower court's opinion as its own.

STATE INSURANCE GUARANTY ASSOCIATIONS' INTEREST IN THE DISPUTE

All fifty states and the District of Columbia have enacted statutes establishing insurance guaranty associations. An insurance guaranty association is a non-profit association of all of the property and casualty insurers licensed in a particular state. An insurance guaranty association's purpose, subject to certain limitations, is to pay the residents of its state who have claims under insurance policies issued by insolvent insurers that were licensed to do business in that state. Upon paying such claims, a guaranty association receives a claim in the insolvent insurer's liquidation proceedings equal to the amount of the claims paid. If the guaranty association is unable to satisfy its claim against the insolvent insurer's estate (in whole or in part), it assesses its member companies by the amount of the short fall and the member companies, in turn, raise their policyholder's premiums to recoup the cost of this assessment. The federal government's assertion that it has a "super-priority" over the claims of other policyholders and the guaranty associations will, therefore, have a substantial impact, not only on the final resolution of Eastern Indemnity's insolvency, but on the liquidation procedures of all fifty-one U.S. guaranty associations.

If the Fourth Circuit opinion is allowed to stand, the decision will adversely affect state insurance liquidation proceedings and diminish policyholder protection in at least two respects:

First, the federal government's asserted priority will cause policyholders of insolvent companies to suffer a lower priority claim with respect to claims not covered by state guaranty associations. All state guaranty associations place limits on the claim amounts subject to guaranty association protection. Some associations may also not cover certain lines of business (such as surety bonds).[1] Claims in excess of guaranty association limits or claims in excluded lines of business can only be collected from the estate of the insolvent insurer.

Second, all state guaranty associations have annual limits on the maximum assessments that may be levied against member companies to pay covered claims. If the federal "super-priority" is upheld, more of the insolvent insurers obligations will be borne by guaranty associations which, in turn, will lower the capacity of the associations to respond to insolvencies. Moreover, the decision will require insurance policyholders generally to bear the added burden of the federal "super-priority."

The Property and Casualty Insurance Guarantee Corporation (the "Maryland Guaranty Corporation") is the in-

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[1] *See* TEX. REV. CIV. STAT. ANN. art. 21.28-C § 1 (Vernon 1987) (surety bonds excluded from the scope of the Texas Property and Casualty Guaranty Association's protection). Other states, including Illinois, have recently amended their guaranty fund statutes to exclude surety bonds. *See* ILL. ANN. STAT. ch. 73, § 1065.83(c) (Smith-Hurd Supp. 1988).

surance guaranty association created under Maryland law.[2] The Illinois Insurance Guaranty Fund (the "Illinois Fund") is the insurance guaranty association created under Illinois law.[3] The Wisconsin Insurance Security Fund (the "Wisconsin Fund") is the insurance guaranty association created under Wisconsin law.[4] The Maryland Guaranty Corporation and the Illinois fund are two of the eight state insurance guaranty associations that will pay claims under surety bonds issued by Eastern Indemnity.[5] The guaranty associations in the other twenty-six states where Eastern Indemnity was licensed provide no coverage at all for claims under surety bonds. Non-governmental bondholders in those states must collect from the estate of the insolvent insurer, or not at all.

Section 158A of the Maryland Insurance Code, like almost all state insurance liquidation statutes, gives guaranty association claims and policyholder claims that are not covered by guaranty associations equal priority. If the Fourth Circuit's decision is allowed to stand, payment of the government's claim will completely exhaust the Eastern Indemnity estate. There will be no assets left to pay the claims of the eight guaranty associations burdened by Eastern Indemnity's insolvency. Moreover, if the government's "super-priority" is allowed, policyholder claims in the twenty-six states where Eastern Indemnity did business and whose guaranty funds do not cover surety bonds will be rendered worthless.

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[2] MD. ANN. CODE art. 48A, § 504 *et seq.* (1986).

[3] ILL. ANN. STAT. ch. 73, § 1065.82 *et seq.* (Smith-Hurd Supp. 1988).

[4] WIS. STAT. ANN. § 646.01 (West Supp. 1986).

[5] The other guaranty associations that will pay claims under surety bonds issued by Eastern Indemnity are: Georgia, Nevada, Texas, Michigan, Louisiana and the District of Columbia.

Guaranty associations are not operated as state agencies and are not funded by state tax revenues. Instead, guaranty associations assess their member insurance companies for the money needed to pay claims. The assessed companies, in turn, recoup the amount of those assessments by charging their policyholders higher premiums. Section 516 of the Maryland Insurance Code, for example, requires members of the Maryland Guaranty Corporation to include in their premiums amounts sufficient to recoup any assessments by that Guarantee association. Similarly, the Illinois courts have expressly recognized that through their premiums, policyholders of solvent companies pay for the Illinois Fund's coverage of the policyholders of insolvent Illinois insurers. *Adams v. The Illinois Insurance Guaranty Fund*, 85 Ill. App. 3d 867, 869, 407 N.E.2d 638, 640 (1980).

To the extent that guaranty associations recover on their claims against insolvent companies, they return those amounts to their members who, in turn, reduce their policyholder's premiums.[6] Everytime a policyholder pays his or her premium to a licensed, *i.e.*, member, company, part of that premium goes to pay the claims of policyholders of insolvent insurers. Therefore, the less a guaranty association is able to recover from the estate of an insolvent insurer, the greater the burden it must place on the policyholders of its members.

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[6] *See* MD. ANN. CODE art. 48A, § 516 (1986):

> The rates and premiums charged for insurance policies and surety bonds . . . shall include amounts sufficient to recoup . . . a sum equal to the amounts paid to the Corporation by the member insurer *less any amounts returned to the member insurer by the Corporation*. . . .

(emphasis added).

If the decision of the Fourth Circuit Court of Appeals is allowed to stand, there will be no assets left to reimburse the eight guaranty associations burdened by Eastern Indemnity's insolvency, and those guaranty associations will be forced to pass on the cost of the claims they cover to the policyholders of their member insurers.

The long-term effect of that decision will be borne by the insurance buying public and as the primary function of this country's guaranty associations is the protection of the insurance buying public, the Amici guaranty associations have a very real interest in seeking this Court's review of the Circuit Court's decision.[7]

TEXAS ANCILLARY RECEIVER'S INTEREST IN THE DISPUTE

James T. Odiorne is the Texas Ancillary Receiver for Eastern Indemnity. Pursuant to the order appointing him ancillary receiver and pursuant to Article 21.28 of the Texas Insurance Code, Mr. Odiorne has taken possession of certain Eastern Indemnity assets located in the State

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[7] *See* MD. ANN. CODE art. 48A, § 504(a)(1) (1986):

> The purposes of this subtitle are to provide a mechanism for the prompt payment of covered claims under certain insurance policies and to avoid financial loss to residents of Maryland who are claimants or policyholders of an insurer, *including surety*, which has become insolvent; and to provide for the assessment of the cost of such payments and protection among insurers.

(emphasis added). *See also* WIS. STAT. ANN. § 646.01(2)(a) (West Supp. 1986). *And see* ILL. ANN. STAT. ch. 73, § 1065.82 (Smith-Hurd Supp. 1988).

of Texas. Mr. Odiorne has the right and duty to use those assets to determine and pay the claims of Eastern Indemnity's Texas policyholders as well as those of the Texas Property and Casualty Insurance Guaranty Association (the "Texas Guaranty Association"). While Mr. Odiorne has the right to use Eastern Indemnity's Texas assets to pay the expenses of the receivership's administration, the Fourth Circuit's decision has effectively exhausted those assets and the costs of the receivership are being covered by the Texas Guaranty Association.

The Fourth Circuit's decision stripped Mr. Odiorne of the assets he was supposed to use to carry out his statutory duty of protecting Texas policyholders. The Circuit Court's holding has left the Texas Ancillary Receiver with insufficient assets to pay the administrative expenses of determining policyholder claims, let alone the assets needed to actually pay those claims. While the Texas Guaranty Fund has "taken up the slack" somewhat, assessing its members to cover the costs of the federal government's asserted claim, the ultimate cost of the Texas Guaranty Fund's rescue will be borne by Texas consumers.

Thus, because of his immediate concern regarding the costs and consequences of Eastern Indemnity's liquidation and his overall concern regarding the potential impact of the Fourth Circuit's decision on future Texas receiverships, the Texas Ancillary receiver has a very real interest in seeking this Court's review of the lower court's decision in this case.

SUMMARY OF ARGUMENT AND REASONS FOR GRANTING THE WRIT

The Maryland Liquidator and these Amici Curiae take the position that the McCarran-Ferguson Act, 15 U.S.C.A. § 1011 *et seq.* (West 1976), both by its express language and its intended purpose, negates the government's "all mine" contention and renders the general provisions of 31 U.S.C.A. § 3713 (West Supp. 1988) inapplicable to this case. The relevant provisions of the McCarran-Ferguson Act are as follows:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (b) *No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance*, or which imposes a fee or tax upon such business, *unless such Act specifically relates to the business of insurance*: Provided, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

15 U.S.C.A. § 1012 (West 1976) (emphasis added).

By holding that the liquidation of an insolvent insurance company does not fall within the McCarran-Ferguson Act's definition of the "business of insurance," the Fourth Circuit's opinion does violence to that Act's intent, purpose and express language; is unfair and inequitable to many

of those involved in government construction work; and misconstrues prior decisions of this Court interpreting that Act in its narrow anti-trust context.[8]

Moreover, a decision by this Court on the issue presented is urgently needed now because:

1) Other federal courts have held that the liquidation of an insolvent insurance company constitutes the "business of insurance" for McCarran-Ferguson Act purposes;[9]

2) The Court of Appeals decision will have a direct impact on all ongoing and future insurance company liquidations wherein the federal government is a claimant—leaving state liquidators shackled with the threat of personal liability for incurring expenses that reduce the government's take, even those expenses necessary to marshall all of the insolvent state's assets;

3) Finally, the Court of Appeals decision threatens more than the liquidation process. The Fourth Circuit's holding that the regulation of such a central aspect of the insurance industry does not constitute the regulation of the "business of insurance" for McCarran-Ferguson Act purposes, calls into question many of the most funda-

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[8] *See* James A. Gordon's Petition for Certiorari in this matter, p.8 n.5 (citing: *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982); *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979) and *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453 (1969)) (hereinafter "Gordon Petition").

[9] *See* Gordon Petition, p.8 n.5 (citing: *Washburn v. Corcoran*, 643. F.Supp. 554 (S.D.N.Y. 1986) and *Idaho ex rel. Soward v. Internal Revenue Service*, 662 F.Supp. 60 (D. Idaho 1987)). Although the latter was recently overturned by the United States Court of Appeals for the Ninth Circuit, that fact merely underscores the need for this Court to review and settle this issue once and for all. *See* 88 Daily Journal D.A.R. 11528 (September 9, 1988).

mental aspects of state insurance regulation and gives the federal government the means to sidestep the McCarran-Ferguson Act in numerous other insurance regulatory contexts. Armed with the Circuit Court's decision, the government will be able to challenge any state insurance law it finds objectionable, establishing in the courts that which to date has been denied by Congress—a federal body of insurance law.

ARGUMENT AND REASONS FOR GRANTING THE WRIT

I.

THIS COURT SHOULD DECIDE WHETHER THE "BUSINESS OF INSURANCE" UNDER THE McCARRAN-FERGUSON ACT IS LIMITED TO THE BUSINESS OF SOLVENT INSURANCE COMPANIES.

The essence of the Fourth Circuit's decision is that the McCarran-Ferguson Act applies only to the regulation of solvent insurance companies. However, neither the McCarran-Ferguson Act itself, common sense, public policy or case law support such a result.

The Maryland Insurance Code's liquidation provisions are part of the overall statutory scheme by which Maryland regulates the business of its insurers. Like every state, Maryland keeps a close watch on its insurance industry—from formation and licensing (MD. ANN. CODE art. 48A, § 42 *et seq.* (1986)) to dealings with policyholders (MD. ANN. CODE art. 48A, §§ 375, 242 (1988)) to the cancellation of policies (MD. ANN. CODE art. 48A, § 240A (1988))

to the rehabilitation and liquidation of insolvent companies, MD. ANN. CODE art. 48A, § 141 (1986).[10]

Subtitle 10 of the Maryland Insurance Code, which governs insolvency and liquidation proceedings against insurers, and section 158A of that subtitle, which gives policyholders priority in the distribution of an insolvent insurer's assets, regulate the "business of insurance" at its most basic and fundamental level, namely paying the claims of policyholders. By governing what this Court has held to be the core of the "business of insurance"—the relationship between an insurer and its policyholders, *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453, 460 (1969), the Maryland liquidation priority statute regulates the very essence of that state's insurance industry.

The mere fact that a liquidator replaces the board of directors of an insurance company should not alter the basic nature of the insurer/insured relationship. If, it does and the McCarran-Ferguson Act applies only to the regulation of solvent companies, that is a far-reaching decision that only this Court should make.

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[10] *See* WIS. STAT. ANN. § 645.01(4)(f) (West 1980) ("The purpose of this chapter is the protection of the interests of insureds, creditors, and the public generally, . . . through . . . *[r]egulation of the insurance business* . . . .") (emphasis added).

II.

THE COURT OF APPEALS DECISION WILL UNFAIRLY DEPRIVE MANY WHO WORK ON GOVERNMENT PROJECTS OF ANY MEANS OF FINANCIAL PROTECTION.

Like most states, Maryland gives the policyholders of an insolvent insurer a priority over all other claimants (with the exception of the liquidator, certain employees, and state and federal tax authorities). MD. ANN. CODE art. 48A, § 158A (1986). Courts which have interpreted similar provisions in other jurisdictions have recognized that this type of priority protects the interests of the insurance buying public—those who most need protecting when an insurer becomes insolvent. *American Re-Insurance, et al. v. Washburn, et al.*, 122 Ill. 2d 555, 566-68, 524 N.E.2d 538, 542-43 (1988). The Fourth Circuit's decision, however, completely ignored this interest and stripped Eastern Indemnity's non-governmental bondholders of the protection they had contracted for and, in many cases, of their state law lien rights as well.

Maryland's priority statute requires *all* of Eastern Indemnity's policyholders to share pro rata in the liquidated assets of that company in accordance with the cardinal rule of liquidation—no member of a class of creditors shall be allowed a preference over the other members of that same class.[11] By thwarting this distribution scheme, the

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[11] *See People v. Cosmopolitan Insurance Company*, 89 Ill. App. 2d 225, 223 N.E.2d 90 (1987):

> The insolvency of an insurance company casts burdens upon its insureds, claimants against its insureds and, if a stock company, against its stockholders. The consequences to those injured are severe. This court cannot, however, . . . seek to lessen the injury of one . . . at the expense of other injured persons . . . .

(Footnote continued on following page)

Fourth Circuit Court completely negated the equitable purpose of that statute and doomed hundreds of contractors, laborers, and materialmen to receive no payment at all on their claims under Eastern Indemnity's surety bonds.

Moreover, many of the claimants who will be denied recovery from the Eastern Indemnity estate are claimants under Miller Act bonds issued by Eastern Indemnity in connection with federally funded construction projects. One type of Miller Act bond is a performance bond designed to protect the government's interests as the owner of a project.[12] Another type of Miller Act bond is a payment bond designed to protect the interests of laborers and materialmen who perform services or provide goods for the benefit of a government owned project.[13] Denying recovery from the Eastern Indemnity estate under this second type of bond is particularly harsh since, under the Miller Act, these laborers and materialmen will also be denied their normal state law lien rights. Because they have no enforceable rights against the federal government and cannot acquire liens on public property, these laborers' and materialmen's only possible source of protection are the Miller Act payment bonds issued by Eastern Indemnity.[14]

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[11] *continued*

Id., at 93. *See also General Reinsurance Corp. v. Missouri General Insurance Co.*, 458 F. Supp. 1, 5 (W.D. Mo. 1977), *aff'd.* 596 F.2d 330 (8th Cir. 1978).

[12] 40 U.S.C.A. § 270a (West 1986).

[13] 40 U.S.C.A. § 270b (West 1986).

[14] *See Ramsdell v. G.H. Coffey Co., Inc.*, 632 F.2d 162, 163 (1st Cir. 1980) (ordinarily, sovereign immunity bars attachment and garnishment of government funds and an unpaid subcontractor's remedy under sections 270a to 270d of this title is a payment bond). *See also U.S. ex rel. B's Co. v. Cleveland Elec. Co. of S.C.*, 373

(Footnote continued on following page)

However, under the Circuit Court's decision, the government will be able to side-step the Maryland insurance laws that would allow these laborers and materialmen the right to share equally with the government in the Eastern Indemnity assets.

III.

MANY OTHER CURRENT INSURER INSOLVENCY PROCEEDINGS, AS WELL AS FUTURE INSOLVENCIES, WILL BE DIRECTLY IMPACTED BY THE CIRCUIT COURT'S DECISION.

The Amici Curiae ask this Court to grant the Petitioner's petition for a writ of certiorari because of the effect that the final resolution of this case will have on a number of insurer insolvency proceedings currently underway as well as on future insolvencies which will undoubtedly occur.

As stated above, Maryland, like most states, has attempted to protect the policyholders of insolvent insurers by giving them a preference in the distribution of those insurers' assets. Giving the federal government a "superpriority" over all other policyholders will disrupt these priority systems and cast doubt upon the protection such statutes actually provide non-government policyholders.

In addition, the Fourth Circuit's decision will have a chilling effect on the conduct of insurer liquidation proceedings. With the Circuit Court's decision in hand, the federal government will continue to use 31 U.S.C.A. § 3713 (West Supp. 1988) to threaten state insurance liqui-

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[14] *continued*

F.2d 585, 589 (4th Cir. 1967) (suit under 270a to 270d of this title is the only remedy for an unpaid subcontractor on a government project; he has no claim or lien against the government).

dators with personal liability if its claims are not paid first. Such threats paralyze liquidators, who fearing personal liability, are hesitant to perform their statutory duties.[15] Moreover, if the federal government's intimidation tactics continue, they will no doubt discourage qualified persons from serving as liquidators.

IV.

THE CIRCUIT COURT'S DECISION FOR THE FIRST TIME CALLS INTO QUESTION WHETHER MANY OF THE MOST FUNDAMENTAL ASPECTS OF STATE INSURANCE REGULATION COME WITHIN THE "BUSINESS OF INSURANCE".

The rationale of the Fourth Circuit's decision places many basic and fundamental aspects of regulating and conducting the business of insurance outside the scope of the McCarran-Ferguson Act's protection. To accept the Circuit Court's view that the only activities which constitute the "business of insurance" (and are thus protected) are those directly connected to underwriting and policy issuance, leads to the conclusion that statutes regulating the formation and licensing of insurers do not regulate the "business of insurance." Yet this fundamental state regulatory power is unquestionably the type of insurance regulation that Congress intended to preserve for the states when it enacted the McCarran-Ferguson Act. Indeed, this Court itself has stated that state laws regulating the licensing

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[15] *See* Affidavit of Fred Nepple dated 9-13-88 (Appendix 1), regarding the federal government's attempt to sue Nepple personally for satisfaction of an Internal Revenue claim against an insolvent insurer Nepple was liquidating. *See also* letter from Harry Eakin (liquidator of Allied Fidelity Insurance Co.) dated 1-13-88 (Appendix 2), informing all state insurance guaranty funds that their claims against Allied Fidelity's estate would not be paid until the issue of the federal government's alleged priority has been resolved.

of insurers are laws regulating the "business of insurance." *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. at 460. *Cf. Robertson v. People of the State of California*, 328 U.S. 440 (1946).

Similarly, the Fourth Circuit's limited interpretation of this phrase would mean that an insurer's dealings with its policyholders (once a policy has been issued) do not constitute the "business of insurance" and that a state's unfair trade practice statutes which govern those dealings do not regulate the "business of insurance" and are not entitled to McCarran-Ferguson protection. *See* MD. ANN. CODE art. 48A, §§ 240A and 227 (1986 and 1988 respectively) (restricting an insurer's right to cancel policies after they have been written and prohibiting insurers from improperly inducing policyholders to cancel their policies).[16] Nothing in this Court's prior decisions interpreting the McCarran-Ferguson Act in its narrow anti-trust context, justifies or supports such a result.[17]

CONCLUSION

While this Court's caseload is severe, the instant case, presenting a pervasive insurance regulatory issue that will have an impact on the rights of insureds and claimants

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[16] Ironically, the District Court which decided the case at bar has itself recognized that Maryland's unfair trade practice provisions regulate the "business of insurance" and are, in fact, entitled to the protection of the McCarran-Ferguson Act. *State of Maryland v. Blue Cross and Blue Shield*, 620 F. Supp. 907, 919-20 (D. Md. 1985). *See also Mathis v. Automobile Club Inter-Insurance Exchange*, 410 F. Supp. 1037, 1040 (W.D. Mo. 1976).

[17] *See supra* note 7 and accompanying text.

in all fifty states and the District of Columbia, merits this Court's review.

Respectfully submitted,

THOMAS W. JENKINS
HUGH C. GRIFFIN *
MARK R. GOODMAN
LORD, BISSELL & BROOK
115 South LaSalle Street
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Counsel for Amici Curiae

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APPENDICES

APPENDIX 1

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, ET AL.,

Respondents.

AFFIDAVIT

STATE OF WISCONSIN
COUNTY OF DANE—ss.

Fred Nepple, being duly sworn upon oath, deposes and says:

1. Affiant is an attorney and employee of the Office of the Commissioner of Insurance of the State of Wisconsin, and at all times pertinent hereto was personally involved in the matters set forth below.

2. In 1975 Wisconsin Surety Corporation was an insurer domiciled in Wisconsin, and was in the business of selling surety bonds.

3. In April 1975 the Office of the Commissioner of Insurance of the State of Wisconsin placed Wisconsin Surety Corporation into liquidation, under the jurisdiction of the Liquidation Court, Dane County Circuit Court, Case No. 146-166.

4. The Court appointed the Wisconsin Commissioner of Insurance as Liquidator.

5. The United States of America, Internal Revenue Service, was one of the claimants in the liquidation estate, with certain specific claims seeking recovery under the provisions of surety bonds issued by the insolvent insurer, and with other specific claims seeking other types of recovery against the insolvent insurer.

6. In May 1984 the liquidation was completed and proceedings were terminated.

7. As of the termination date, the Liquidator pursuant to Wisconsin insurance liquidation law had paid none of the claims of the United States of America seeking recovery under the surety bond provisions.

8. In February 1985 representatives of the Office of the Commissioner of Insurance for the State of Wisconsin were notified that the United States of America was considering an action against the Commissioner, and that it asserted priority for all unpaid claims under Title 31, U.S.C. § 3713, and that it asserted personal liability against the Commissioner under Title 31, U.S.C. § 3713.

9. The aggregate amount of all claims and interest sought by the United States of America was approximately $200,000.

10. The liquidation proceedings were reopened, and a settlement was reached in 1987.

11. All facts set forth above in paragraphs 1-8 and 10 are filed with the Liquidation Court as a matter of public record in such Case No. 146-166.

/s/ FRED NEPPLE

Subscribed and sworn to
before me this 13th day
of September, 1988.

/s/ _____

Notary Public, Dane County
Wisconsin
My Commission: is permanent.

STATE OF WISCONSIN
CIRCUIT COURT
DANE COUNTY

In the Matter of the Liquidation of
WISCONSIN SURETY CORPORATION,
a Wisconsin Insurance Corporation.

REPORT ON CLAIM AND ORDER
CD #425A, B & C
CD #436A, B & C
Case No. 146-166

The Liquidator hereby reports to the Court regarding the above claim.

STATEMENTS BY CLAIMANT

The undersigned, being sworn, under the cooperation and perjury provisions of the Wisconsin Statutes states that:

1. The name and address of claimant is:
United States
Internal Revenue Service
U.S. Department of Justice, Tax Division
Washington, D.C. 20530

2. On the date of the insured event or on April 11, 1975 claimant was not [strike if appropriate] a resident of the State of Wisconsin (or a corporation organized under Wisconsin law).

[3. Claimant has not [strike if appropriate and furnish all pertinent details] received or acquired a preference, lien, conveyance, transfer, assignment or encumbrance voidable under Chapter 645, Wisconsin Statutes; and claimant does not [strike if appropriate and furnish all pertinent details] *hold security relating to this matter.]**

[4. Claimant has exerted and will continue to exert every reasonable effort to minimize any loss which is the subject of this claim, and to date has not [strike if appropriate and furnish all pertinent details] *received any payment regarding such loss; and claimant immediately will report to the Liquidator any such payment received subsequent to this date.]*

5. In consideration of the recommendation of the Liquidator of Wisconsin Surety Corporation regarding payment of part or all of the claim of the claimant bearing the above court docket number, the claimant hereby for himself, his heirs, executors, administrators and assigns, (or for itself, its successors and assigns) does remise, release and forever discharge such Liquidator and the Wisconsin Commissioner of Insurance each individually and in his official capacity, his heirs, executors, administrators, assigns and successors in office, and the estate of the Wisconsin Surety Corporation, from any and all right, cause of action, claim or demand of whatsoever kind, nature or description at law or in equity or created by statute which the claimant now has or which his heirs, executors, administrators or assigns (or its successors or assigns) can, shall, or may hereafter have.

6. Claimant hereby stipulates his approval of the determination by the Liquidator as set forth herein.

/s/ JEFFREY D. SNOW
Signature of person authorized
to act for claimant

* Bracketed and italicized portions throughout were stricken in the original copy.

[On this ____ day of _____, 19____, before me personally appeared _____ to me personally known and known to be the same person described in and who executed the foregoing instrument and who duly acknowledged to me that he executed the same.]

On this 11th day of March, 1987, before me personally appeared Jeffrey D. Snow, to me known to be the person who executed the foregoing instrument, and to me known to be the attorney for said [Corporation], entity, and acknowledged that he executed the foregoing [as such officer as the deed of said Corporation] by its authority.

[Strike non-applicable paragraph]

(Notarization omitted in printing.)

STATEMENTS BY LIQUIDATOR

6. The claimant filed a written proof of claim which is deemed to have been timely filed in substantial compliance with Wis. Stats. §645.61 and which has received from this Court the above docket numbers.

7. The particulars of such claim and the amount claimed are as follows:

See attached.

8. The amount allowed in the determination by the Liquidator as set forth below does not exceed the amount of the bond under which this claim is made.

DETERMINATION BY LIQUIDATOR

WHEREFORE, on the basis of the foregoing and the records and data in the possession of the Liquidator and related investigation, the Liquidator hereby:

1) Recommends *[(reports)]* the allowance of the above-described claim in the amount of $28,102.33, with the amount allowed to be eligible for distribution to the claimant as follows: in Class 3 the amount of $24,128.53, *[in Class ____ the amount of $_____, in Class ____ the amount of $_____]* and in Class 5 the amount of $3,973.80, *[all pursuant to Wis. Stats. § 645-68 on a pro rata basis with all other approved claims in the above liquidation proceeding.]*

[(2) Recommends the disallowance in full of the above-described claim.]

Dated: March 17th, 1987

LIQUIDATOR OF
WISCONSIN SURETY CORPORATION

By: /s/ CHRISTOPHER J. WILCOX

P.O. Address:

LaFollette, Sinykin, Anderson & Munson
Suite 300, 222 W. Washington Avenue
Madison, Wisconsin 53703

ORDER

Upon this record herein and the foregoing Report of the Liquidator and being fully advised in the premises, the Court by this Order hereby:

(1) Determines that the loss claim settlement as recommended for allowance is a loss for which Wisconsin Surety Corporation is liable, and accordingly approves such recommendation and allows payment of such loss claim settlement in the amount recommended by the Liquidator.

[(2) Approves such recommendation and disallows such claim in its entirety.]

[(3) Disapproves and modifies such recommendation as set forth in the attached Determination on Report or Claim.]

Distribution to the claimant of the amount allowed shall be according to the priorities recommended by the Liquidator.

[Portions of the amount allowed are eligible for distribution to the claimant in a class or classes lower in priority than Class 3. It is anticipated at this time that there will be insufficient assets to make any distribution to claimants in classes lower in priority than Class 3 and therefore that the above claimant will receive no distribution whatsoever regarding any portions eligible for distribution in Classes 4, 5, 6, 7, 8, 9, 10 and 11 inclusive, and that such claimant will receive no further notice regarding such portions.]

Dated: March 17th, 1987

BY THE COURT:

/s/ _____
Circuit Court, Branch 4
Dane County, State of Wisconsin

ATTACHMENT – C.D. 425A, B & C
and 436A, B & C

The claimant seeks recovery of $3,973.80, plus interest, for unpaid tax-related moneys alleged to be due directly from the insolvent insurance company, Wisconsin Surety Corporation. This claim is comprised of $3,281.74 (Claim 425C) for withholding and Federal Insurance Contribution Act taxes due from Wisconsin Surety Corporation; and of $692.06 (Claim 436C) for withholding due from Wisconsin Surety Corporation.

The claimant also seeks recovery of $50,854.14, plus interest, for actions taken by Wisconsin Surety Corporation under the provision of certain surety bonds issued by the insurer. This claim is comprised of $7,318.27 (Claim 425A) against Wisconsin Surety Corporation as surety for LTL Electrical Contractors, Inc.; $12,548.57 (Claim 425B) against Wisconsin Surety Corporation as surety for E. C. Construction Co., Inc.; $13,196.89 (Claim 436A) against Wisconsin Surety Corporation as surety for V & L Construction Co., Inc.; and $17,790.41 (Claim 436B) against Wisconsin Surety Corporation as surety for Vankeirsbelk Construction Company.

Claims 425A, 425B, 425C and 436B were disallowed by the Liquidator on June 18, 1980. The disallowance was mailed to the claimant, and no objection having been filed within 60 days, the Court ordered the claims disallowed on September 9, 1980. Claim 436A was disallowed by the Liquidator on June 18, 1980. The determination was mailed to the claimant, and no objection having been filed within 60 days, the Court disallowed the claim on September 12, 1980. Claim 436C was allowed in full by the Court on February 29, 1980, but the check issued to the claimant by the Liquidator in full payment has never been cashed and is now void.

On May 29, 1984 the liquidation proceedings were terminated. On or about February 6, 1985 representatives of the Office of the Commissioner of Insurance for the State of Wisconsin were notified that the claimant was

considering bringing an action against the Commissioner in federal court, asserting priority under Title 31, U.S.C. § 3713, and also asserting liability to the claimant under Title 31, U.S.C. § 3713. On February 18, 1987 the proceedings were reopened.

The claimant and the Liquidator have reached a formal settlement, by which the Liquidator has agreed to pay the claimant a total of $28,102.33, in return for a full release, in compromise of these disputed claims.

Accordingly, Claims 425A, 425B, 436A and 436B are allowed as class 3 claims, with the total amount for the four claims to be paid being $24,128.53; and Claims 425C and 436C are allowed in full as class 5 claims, with the aggregate amount to be paid being $3,973.80; for a total settlement to be paid forthwith to the claimant in the amount of $28,102.33.

Q:425.436

APPENDIX 2

Allied Fidelity Insurance Co.

IN LIQUIDATION

TO: ALL STATE INSURANCE COMMISSIONERS, SUPERINTENDENTS AND DEPARTMENTS, ALL ANCILLARY RECEIVERS, AND ALL STATE INSURANCE GUARANTY FUNDS OR ASSOCIATIONS

FROM: INDIANA INSURANCE COMMISSIONER HARRY E. EAKIN, AS LIQUIDATOR OF ALLIED FIDELITY INSURANCE CO. ("AFIC")

DATE: JANUARY 13, 1988

RE: ALLEGED FEDERAL PRIORITY

Last September, the AFIC Liquidator sent to you an accounting, a duplicate copy of which is enclosed, which mentioned the uncertainty created by alleged federal priorities in the AFIC liquidation proceeding. See paragraphs 6 and 13 of the accounting. The uncertainty was heightened by the recent federal court decision in the Eastern Indemnity liquidation in Maryland. A copy of that decision is also enclosed.

While the AFIC Liquidator is still in the process of analyzing the thousands of claims received by the December 1 claim filing deadline, it looks as if the federal claims received will total in excess of $7 million. That being so, and until the AFIC Liquidator has had a chance to compile sufficient information to prepare a more complete report to the Court, each insurance department, ancillary receiver, and guaranty fund should make certain that no assets of AFIC

are used in a way that would arguably subject insurance departments, receivers or guaranty funds to the contention that the claimed federal priority has been violated. Obviously, departments, ancillary receivers or guaranty funds that are holding special deposits or other assets of AFIC need to be the most careful.

No. 88-302

Supreme Court, U.S.
FILED
SEP 16 1988
JOSEPH F. SPANIOL, JR.
CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, SPECIAL DEPUTY, STATE INSURANCE COMMISSIONER OF MARYLAND AND RECEIVER, EASTERN INDEMNITY COMPANY OF MARYLAND IN RECEIVERSHIP,
Petitioner,

vs.

UNITED STATES DEPARTMENT OF THE TREASURY, W.E. DOUGLAS, COMMISSIONER, UNITED STATES DEPARTMENT OF THE TREASURY, FISCAL SERVICE,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS AS AMICUS CURIAE IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS AS AMICUS CURIAE IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

INTEREST OF THE AMICUS CURIAE

The National Association of Insurance Commissioners ("NAIC") is a nonprofit, unincorporated association whose membership consists of the 50 states, the District of Columbia, the territories and insular possessions of the United States. The NAIC was organized in 1871 to assure the protection of policyholders across the country. As stated in the NAIC's Constitution, the protection of policyholders continues to be the principal objective of the NAIC:

Article II. OBJECTIVE

The objective of this body is to serve the public by assisting the several State insurance supervisory officials, individually and collectively, in achieving the following fundamental insurance regulatory objectives:

(1) Maintenance and improvement of State regulation of insurance in a responsive and efficient manner;

(2) Reliability of the insurance institution as to financial solidity and guaranty against loss;

(3) Fair, just and equitable treatment of policyholders and claimants.

I *NAIC Proceedings* p. iii (1988).

The principal function of the NAIC is to serve the public by assisting these insurance commissioners in overseeing the activities of the insurance industry, which activities include the supervision of rehabilitation and liquidation proceedings.

Each commissioner is obligated by law to protect policyholders and in doing so, must carry out all applicable statutory procedures. At issue in this case is whether the Maryland statutory procedures setting forth a priority system for claims payment constitute statutes enacted for the purpose of regulating the "business of insurance" under the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*,[1] and if so, whether this precludes application of the "super" priority set forth in 31 U.S.C. § 3713[2] to the claims in this liquidation.

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1. Appendix A.
2. Appendix B.

The Maryland statutes are derived from a model law developed by the NAIC, the Insurers Supervision, Rehabilitation and Liquidation Model Act, which has been adopted in some manner by every state. This model law places the claims of policyholders above those of the state or federal government. All states which have adopted this approach are significantly affected by the decision of the Fourth Circuit Court of Appeals, which held that claims of the federal government must be placed ahead of policyholder claims. The individual state commissioners, the members of the NAIC, possess a vital interest in the outcome of this matter because the opinion of the Circuit Court diminishes the scope of state regulation of the business of insurance. This impairs the ability of the commissioners to fulfill the responsibility vested in them by law to wind up the affairs of insolvent insurance companies, which responsibility includes the paying of policyholder claims.

In submitting this brief, the NAIC seeks to demonstrate its interests in this proceeding, which are:

1. To preserve the orderly disbursement of assets of insolvent insurers,
2. To encourage cooperation and uniformity among states in the liquidation of insolvent insurers, and
3. To assist the state insurance commissioners in protecting the interests of policyholders across the country.

This brief is therefore submitted, with consent of the parties, in support of the petition of the receiver of Eastern Indemnity Company of Maryland.

ARGUMENT

I. The Fourth Circuit's decision creates a significant nationwide impact on all state insurance commissioners in the administration or supervision of insolvent insurance companies.

A. The priority scheme for payment of claims which was developed by the NAIC has been widely adopted by the states and exists to protect policyholders.

In urging this Court to grant the receiver's petition, the NAIC seeks to maintain the orderly and uniform distribution of the assets of insolvent insurers. The distribution process will be severely hampered if the Fourth Circuit's decision[3] stands because it will destroy the distribution approach taken by the majority of states.

Maryland's statutory scheme governing liquidation proceedings[4] is patterned after the NAIC model concerning the liquidation of insurers.[5] The majority of states have endorsed the priority scheme set forth therein which places policyholder claims before those of the federal government.[6] This is significant because it reflects how fundamental the protection of policyholders is.

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3. *Gordon v. United States Treasury*, 846 F.2d 272 (4th Cir. 1988).

4. Md. Code Ann. Art. 48A, § 132 *et seq.*

5. The Insurers Supervision, Rehabilitation and Liquidation Model Act, Model No. 555, II *NAIC Model Laws, Regulations and Guidelines* (1988).

6. *See* Appendix C for the text of the priority scheme and Appendix D for a list of those states which have adopted this concept.

If the Fourth Circuit Court's decision is allowed to stand, it will directly impair the states' ability to pay policyholder claims. This impairment will extend nationwide, thereby depriving policyholders across the country of the protection afforded to them by the state priority of distribution laws.

The effect of the Fourth Circuit's opinion also extends to the personal liability of the commissioners as receivers or liquidators of insolvent companies because subsection (b) of 31 U.S.C. § 3713 subjects them to liability if they pay any debts before those of the federal government. The state insurance commissioners generally are obligated by law to appoint a receiver or liquidator to handle the affairs of an insolvent insurance company. However, the commissioners' responsibility does not conclude once a receiver or liquidator is appointed. The commissioner always maintains a degree of supervisory responsibility over the activities of the receiver or liquidator. Therefore, whether directly, or indirectly through appointment of a liquidator, the commissioner is ultimately the overseer of the company's affairs. The orderly administration of insolvent company affairs has already been thwarted in a number of instances because of the dilemma facing state commissioners as liquidators of the companies. The dilemma which the commissioners face is whether to release assets of the company to pay claims of the federal government (in contravention of the state priority scheme and in disregard for the interests of policyholders) or to refuse to release the funds and face personal liability for failure to do so. Either of these alternatives is highly undesirable because the interests of the policyholders are ultimately affected. The policyholders face a delay in claims payment, and possibly no payment at all, as a result of the federal claim for priority.

B. The Fourth Circuit failed to take the philosophy of protecting policyholders into consideration when it rendered its decision.

Placing policyholder claims among those paid first coincides with the fundamental philosophy underlying state insurance regulation. That fundamental tenet is to protect the interests of policyholders. Protecting the interests of policyholders has historically been linked to the monitoring of company solvency. As the NAIC's constitution provides, "[t]he objective of this body is to serve the public by assisting the several State insurance supervisory officials . . . in achieving . . . (2) reliability of the insurance institution as to *financial solidity and guaranty against loss;* . . ." (Emphasis added.) The ability of a company to guaranty against loss depends on its financial solidity. That "guaranty against loss" is a protection purchased by a policyholder and it is something which the policyholder is entitled to expect, regardless of the company's financial position.

In the event that a company becomes insolvent and is unable to fulfill its obligations to policyholders, the state steps in and attempts to fulfill those obligations to the extent possible under the law. The "laws" on liquidation originated decades ago. One of the bases for state laws on liquidation is the NAIC's model on liquidation of insurers.[7] This development of model legislation is one of the methods to encourage cooperation and uniformity among the states in the liquidation process, and it is intended to result in protection of policyholder interests. The Fourth Circuit Court failed to take this fundamental philosophy

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7. I *NAIC Proceedings* 30-32 (1936). The model was revised extensively in 1978 and continues to be updated. I *NAIC Proceedings* 238-290 (1978).

of protecting policyholders into consideration when it determined that the state's liquidation process is not the "business of insurance."

C. The Fourth Circuit's decision will affect a number of pending liquidation proceedings.

The issue presented in the receiver's petition is one of widespread significance. It merits review by this Court because of the number of pending insurance company liquidations in which the question is or may become an issue. There are over 30 liquidations currently in process in which the federal priority question has already been or is likely to be raised. In these liquidations alone, it is estimated that over $30,000,000 worth of federal claims may be asserted pursuant to 31 U.S.C. § 3713. In several instances the assets of the insolvent company are insufficient to pay both the claims of the federal government and have anything remaining for policyholders and other insureds. In addition, the commissioners in all states are gravely impeded in their ability to proceed with an orderly distribution of assets until this matter is finally resolved. The ambiguity created by the Fourth Circuit's decision needs to be settled in order for these pending liquidation proceedings to move forward.

II. The Fourth Circuit Court erred in concluding that state regulatory schemes governing liquidation of insolvent insurance companies do not constitute regulation of the business of insurance under the McCarran-Ferguson Act.

The NAIC urges this Court to review the conclusions drawn by the Fourth Circuit that state regulatory schemes governing the liquidation of insolvent insurance

companies do not constitute the business of insurance under the McCarran-Ferguson Act. Whether the members of the NAIC, the insurance commissioners, continue to carry out this obligation of liquidating companies is dependent on resolution of this issue. The states have long followed the mandates of the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, that the regulation of the business of insurance is vested in the states. A ruling that restricts the scope of state regulation of the business of insurance will have a detrimental effect on the insurance commissioners' authority to administer the affairs of insolvent companies across the country. The Fourth Circuit's ruling is not limited to the narrow issue of affording priority to the federal government. If the Fourth Circuit Court's opinion stands, insurance commissioners will not only be forced to relegate payment of policyholder claims to those of the federal government, but their overall authority to administer the insolvency of an insurance company is placed into question because of the ruling that these activities do not constitute the business of insurance under the McCarran-Ferguson Act.

The NAIC requests that this Court re-examine whether the process of liquidating insolvent insurance companies satisfies the test set forth in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982). If the Court should agree with the Fourth Circuit that the *Pireno* three-part test is the appropriate tool for resolving the issue, the NAIC is confident that the criteria to determine whether an activity constitutes the business of insurance will have been satisfied. Under *Pireno*, three factors are relevant: (1) whether the activity involves the transfer or spreading of risk, (2) whether it involves the relationship between an insurer and insured, and

(3) whether the activity is confined to entities within the insurance industry. Concluding that the first factor may not be an indispensable requirement in all cases, the Fourth Circuit Court adopted the district court's analysis that the liquidation of insolvent insurers constitutes regulation of the business of "insurers" rather than the business of "insurance." The NAIC respectfully urges this Court to carefully examine the Fourth Circuit's analysis of whether the three-part *Pireno* test is satisfied in light of the following.

1. Transfer or spreading of risk.

The Fourth Circuit's failure to extend the "business of insurance" to the liquidation process limits the "spreading of risk" to the period preceding, but not including, insolvency. It is the policyholder's risk or exposure which is at issue here—not the risk of insolvency as the Fourth Circuit concluded. The risk to the policyholder does not automatically cease to exist when a company becomes insolvent. The liquidation of the company inextricably involves the payment of claims which this Court itself has recognized as the business of insurance.[8] Limiting the "spreading of risk" to the period preceding insolvency does not coincide with the principal goal of state insurance regulation, which is the protection of policyholders. Undue hardship should therefore not be inflicted on the policyholders of an insolvent insurance company. The policyholder should not be burdened with the responsibility of ascertaining the financial condition of the company prior to the placing of his or her business with that company.

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8. *Group Life and Health Ins. Co. v. Royal Drug Co., Inc.*, 440 U.S. 205, 213 (1979).

A state insurance commissioner undertakes an obligation of administering the affairs of a company if necessary, which may include supervision, rehabilitation or liquidation of the company's affairs. This duty exists from the moment a company receives authorization to conduct business in any given state and extends through the moment the business is finally resolved. This duty is explicitly set forth in state statutes governing the liquidation of insolvent companies.[9] The fact that the states have anticipated that a company may become insolvent and have provided for uninterrupted regulation if insolvency occurs demonstrates that this activity constitutes the business of insurance.

2. Relationship between the insurer and insured.

The Fourth Circuit's opinion fails to address the significance of the state's recognition that the insurer/policyholder relationship continues to exist until the affairs of the company are resolved. The relationship between the insurer and insured/policyholder is specifically addressed in the NAIC model law governing liquidations and is addressed in every state statute governing this process. The fact that the states have anticipated and have prepared for the distribution of money to pay policyholder claims (by statute) demonstrates that the relationship between the insurer and policyholder continues to exist. The statutes were designed to insure that this insurer/policyholder relationship would be disrupted as little as possible in the event of insolvency.

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9. *See e.g.* Md. Code Ann. Art. 48A §§ 132, 134, 135.

3. Activity is confined to entities within the insurance industry.

The NAIC asserts that the Fourth Circuit failed to fully analyze whether liquidation proceedings are confined to the insurance industry. Insurance company insolvencies are not governed by bankruptcy law, but by state insurance statutes governing liquidations. *Universal Marine Ins. Co. v. Beacon Ins. Co.*, 768 F.2d 84, 88 (4th Cir. 1985). These state statutes are only designed to cover insurance company insolvency, and the authority vested therein is limited to the matters involving members of the insurance industry. A review of this third aspect of the *Pireno* test would reveal that this criteria is satisfied as well.

An examination by this Court of these three *Pireno* factors is imperative because it would reveal that the activities at issue in this case do indeed constitute the business of insurance.

III. The Fourth Circuit's decision conflicts with other decisions on the scope of the state commissioners' authority to liquidate insolvent insurance companies.

The Fourth Circuit's opinion is in direct conflict with that issued by a federal district court in *Washburn v. Corcoran*, 643 F.Supp. 554 (S.D.N.Y. 1986), in which the court held that liquidation proceedings constitute the business of insurance. In addition, the Ninth Circuit recently issued a decision in *Idaho v. Internal Revenue Service*, 662 F.Supp. 60 (D. Idaho 1987), *rev'd* No. 87-4057 (9th Cir. filed Sept. 7, 1988), which conflicts with the Fourth Circuit's conclusion that statutes governing liquidation proceedings do not constitute the business of insur-

ance. Although the Ninth Circuit narrowly limited its decision to the issue of whether the state priority scheme should be superseded by the federal statute, 31 U.S.C. § 3713, the court emphasized that the remainder of the Idaho state liquidation statutes are still operative. Under this decision, states are clearly responsible for liquidating insolvent insurance companies. This responsibility is not, however, clear as a result of the Fourth Circuit's opinion which ruled that the Maryland liquidation statutes do not constitute the business of insurance. It is imperative that this uncertainty about the states' overall authority to supervise liquidations be resolved.

SUMMARY OF ARGUMENT

The NAIC vigorously supports the receiver's petition to this Court requesting a clarification of the law concerning the application of the McCarran-Ferguson Act to state liquidation proceedings. Resolution of this issue is urgent in light of conflicting opinions between the Fourth Circuit and the Ninth Circuit. The impact of the Fourth Circuit's opinion on pending liquidations and on state insurance commissioners nationwide requires a review of that decision.

CONCLUSION

The NAIC respectfully requests that this Court grant the receiver's petition for a writ of certiorari.

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September, 1988

APPENDIX

APPENDIX A

McCarran-Ferguson Act

Chapter 20. REGULATION OF INSURANCE

§ 1011. Declaration of policy

Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

§ 1012. Regulation by State law; Federal Law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided,* that after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

§ 1013. Suspension until June 30, 1948, of application of certain Federal laws; Sherman Antitrust Act applicable to agreements to, or acts of, boycott, coercion, or intimidation

(a) Until June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.

§ 1014. Applicability of National Labor Relations Act and Fair Labor Standards Act of 1938

Nothing contained in this chapter shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935, as amended, known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938, or the Act of June 5, 1920, known as the Merchant Marine Act, 1920.

§ 1015. Definition of "State"

As used in this chapter, the term "State" includes the several States, Alaska, Hawaii, Puerto Rico, Guam, and the District of Columbia.

APPENDIX B

31 U.S.C. § 3713

§ 3713. Priority of Government claims

(a)(1) A claim of the United States Government shall be paid first when—

(A) A person indebted to the Government is insolvent and—

(i) the debtor without enough property to pay all debts makes a voluntary assignment of property;

(ii) property of the debtor, if absent, is attached; or

(iii) an act of bankruptcy is committed; or

(B) the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.

(2) This subsection does not apply to a case under title 11.

(b) A representative of a person or an estate (except a trustee acting under title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government.

APPENDIX C

NAIC Insurers Supervision, Rehabilitation and Liquidation Model Act

Section 42. Priority of Distribution

The priority of distribution of claims from the insurer's estate shall be in accordance with the order in which each class of claims is herein set forth. Every claim in each class shall be paid in full or adequate funds retained for such payment before the members of the next class receive any payment. No subclasses shall be established within any class. The order of distribution of claims shall be:

A. Class 1. The costs and expenses of administration, including but not limited to the following:

(1) the actual and necessary costs of preserving or recovering the assets of the insurer;

(2) compensation for all services rendered in the liquidation;

(3) any necessary filing fees;

(4) the fees and mileage payable to witnesses;

(5) reasonable attorney's fees;

(6) the reasonable expenses of a guaranty association or foreign guaranty association in handling claims.

B. Class 2. Debts due to employees for services performed to the extent that they do not exceed $1,000 and represent payment for services performed within one year before the filing of the

petition for liquidation. Officers and directors shall not be entitled to the benefit of this priority. Such priority shall be in lieu of any other similar priority which may be authorized by law as to wages or compensation of employees.

C. Class 3. All claims under policies for losses incurred, including third party claims, all claims against the insurer for liability for bodily injury or for injury to or destruction of tangible property which are not under policies, and all claims of a guaranty association or foreign guaranty association. All claims under life insurance and annuity policies, whether for death proceeds, annuity proceeds, or investment values shall be treated as loss claims. That portion of any loss, indemnification for which is provided by other benefits or advantages recovered by the claimant, shall not be included in this class, other than benefits or advantages recovered or recoverable in discharge of familial obligation of support or by way of succession at death or as proceeds of life insurance, or as gratuities. No payment by an employer to his employee shall be treated as a gratuity.

D. Class 4. Claims under nonassessable policies for unearned premium or other premium refunds and claims of general creditors.

E. Class 5. Claims of the federal or any state or local government. Claims, including those of any governmental body for a penalty or forfeiture, shall be allowed in this class only to the extent of the pecuniary loss sustained from the act, transaction, or proceeding out of which the penalty or for-

feiture arose, with reasonable and actual costs occasioned thereby. The remainder of such claims shall be postponed to the class of claims under Subsection H.

F. Class 6. Claims filed late or any other claims other than claims under Subsection G and H.

G. Class 7. Surplus or contribution notes, or similar obligations, and premium refunds on assessable policies. Payments to members of domestic mutual insurance companies shall be limited in accordance with law.

H. Class 8. The claims of shareholders or other owners.

APPENDIX D

The following states have adopted the principle of paying policyholder claims before those of the federal government:

Alaska Stat. §§ 21.78.180 and 21.78.260 (1978); Ariz. Rev. Stat. Ann. §§ 20-629 (1982) and 20-637 (1984); Ark. Stat. Ann. § 23-68-126 (1988); Conn. Gen. Stat. § 38-462 (1980); Fla. Stat. § 631.271 (1987); Ga. Code Ann. § 33-37-20 (1986); Idaho Code § 41-3342 (1981); Ind. Code § 27-9-3-40 (1979); Iowa Code § 507C.42 (1988); Kan. Stat. Ann. § 40-3601 (1986); Ky. Rev. Stat. § 304.33-430 (1982); La. Rev. Stat. Ann. § 22:746 (1987); Maine Rev. Stat. Ann. tit. 24-A § 4379 (1980); Md. Code Ann. Art. 48A § 158A (1987); Mich. Comp. Laws § 500.7834 (1984); Minn. Stat. § 60B.44 (1987); Mont. Code Ann. § 33-2-1371 (1979); Neb. Rev. Stat. § 44-127.25 (1984); Nev. Rev. Stat. § 696B.420 (1980); N.H. Rev. Stat. Ann. § 402-C:44 (1987); N.M. Stat. Ann. § 59A-41-44 (1984); N.Y. Ins. Law § 7435 (1985); N.C. Gen. Stat. § 58-155.15 (1987); Ohio Rev. Code Ann. § 3903.42 (1983); Okla. Stat. tit. 36 § 1927 (1983); Pa. Cons. Stat. § 40-11-426 (1982); R.I. Gen. Laws § 27-14-22 (1987); S.C. Code Ann. § 38-27-610 (1988); Tenn. Code Ann. § 56-9-127 (1981); Tex. Ins. Code Ann. § 21.28-B (1984); Utah Code Ann. § 31A-27-335 (1986); V.I. Code Ann. tit. 22 § 1277 (1985); W. Va. Code § 33-10-19a (1985); Wis. Stat. § 645.68 (1980); and Wyo. Stat. § 26-28-125 (1983).

(4)

No. 88-302

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OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

—v.—

UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*,

Respondents.

BRIEF *AMICUS CURIAE* OF JAMES P. CORCORAN, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR, IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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This brief amicus curiae is respectfully submitted on behalf of James P. Corcoran, Superintendent of Insurance of the State of New York, as Liquidator of eleven insolvent insurance companies domiciled in the State of New York: American Consumers Insurance Company, American Fidelity Fire Insurance Company, Carriers Casualty Company, Constellation Reinsurance Company of New York, Dominion Insurance Company, Midland Insurance Company, Nassau Insurance Company, Northumberland General Insurance Company (U.S. Branch) and Union Indemnity Insurance Company of New York. Pur-

suant to Rule 36 of the Rules of this Court, amicus has obtained and filed herewith the written consents of each of the parties to the filing of this brief. Amicus supports the petition of the Maryland Deputy Commissioner for a writ of certiorari to review the decision of the Court of Appeals for the Fourth Circuit in this case.

INTEREST OF THE AMICUS CURIAE

Amicus is the Superintendent of Insurance of the State of New York in his capacity as domiciliary liquidator of eleven insolvent insurance companies chartered by or having their United States domicile in the State of New York. These insurance companies are being liquidated in the courts of the State of New York under provisions of New York's statute governing the rehabilitation and liquidation of insolvent insurance companies, Article 74 of the New York Insurance Law, N.Y. Insurance Law §§ 7401, *et seq.* (McKinney 1985 and Supp. 1988). New York's insurance insolvency law, which embodies the Uniform Insurers Liquidation Act, 13 U.L.A. 328 (1986), is similar in many respects to the provisions of the Maryland Code under which the Petitioner herein is liquidating Eastern Indemnity Company of Maryland. In addition, the Superintendent of Insurance acts as rehabilitator of New York-domiciled insurance companies whose financial condition is impaired, and as ancillary receiver or conservator of insurance companies that are domiciled in other jurisdictions and are undergoing insolvency or delinquency proceedings in those jurisdictions. Altogether, as of the most recent period for which statistics are available, amicus as liquidator, rehabilitator, or receiver was responsible for the administration of proceedings in the New York courts involving 36 insurance companies with total reported assets of over $515 million. Definitive resolution of the impact of the federal priority statute, and the wider issue of the application of the McCarran-Ferguson Act to state insurance insolvency systems, is of the first importance to amicus, and to the policyholders of the insurance companies undergoing liqui-

dation in the New York courts under the administration of amicus as liquidator.

SUMMARY OF ARGUMENT

The writ of certiorari sought by Petitioner should be granted to decide whether under the McCarran-Ferguson Act, 15 U.S.C. §§ 1011 *et seq.* (1982), the specific provisions of state statutes regulating the liquidation of insurance companies may be superseded by a federal law of general application like the federal priority statute, 31 U.S.C. § 3713 (1982). Federal courts sitting in New York, including the Federal Court of Appeals for the Second Circuit, have ruled that the McCarran-Ferguson Act permits New York's insurance insolvency statute to operate free of federal interference. These courts have recognized that in New York, as in other states, the liquidation of insolvent insurance companies is the final chapter in a comprehensive scheme of state regulation of the business of insurance. The ruling of the Fourth Circuit below, holding that Maryland insurance insolvency provisions are not protected under the McCarran-Ferguson Act, raises a conflict among the circuit courts that requires resolution.

ARGUMENT

The applicability of the McCarran-Ferguson Act is vital to state insurance insolvency proceedings.

Amicus, as liquidator of insolvent insurance companies in New York, strives to discharge his duties in conformity with applicable law, both state and federal. The New York Insurance Law very specifically governs procedure and substance in insurance liquidation proceedings. For example, the New York Court of Appeals has construed Article 74 of the New York Insurance Law to confer exclusive jurisdiction of all property of and all claims for and against an insolvent company in liquidation on a single state court—the liquidation court. *Knickerbocker Agency, Inc.* v. *Holz*, 4 N.Y.2d 245, 149 N.E.2d 885,

173 N.Y.S.2d 602 (1958). Article 74 establishes, *inter alia*, detailed provisions for the appointment of the Superintendent of Insurance as liquidator (N.Y. Insurance Law § 7405), for the recovery of preferences and other voidable transfers (§ 7425), for offsets (§ 7427), for the disposition of assets and the compromise of claims (§ 7428), for the proof and allowance of claims (§ 7433), and for distribution of assets according to a scheme of priorities established by statute (§§ 7413, 7426, 7434), all under court supervision and pursuant to appropriate court orders.

In satisfying his statutory obligations as liquidator, the Superintendent of Insurance as liquidator has relied on repeated rulings of the federal courts sitting in New York which have held that New York's insurance insolvency system is an integral part of the state scheme of insurance regulation, protected from interference by other federal statutes under Section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b)(1982).[1] This integrated, unified system would be disrupted by the interjection of federal statutes, such as that in issue here, which do not purport to regulate the business of insurance.

New York's insurance insolvency statute, like similar laws in Maryland and other states, occupies a crucial place in a comprehensive scheme designed to protect the public interest in the fiscal responsibility of insurers and their ability to meet their obligations to policyholders. Among the matters dealt with by the New York Insurance Law, Section 307 (McKinney 1985 & Supp. 1988) requires licensed insurers to render annual statements and Section 310 (McKinney 1985) requires them to submit to periodic examinations of their financial condition. In the event a New York-chartered insurer encounters financial difficulties, a range of remedies may be applied, including court-supervised rehabilitation (§§ 7402-7403) and, where nec-

---

1 "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, . . . unless such Act specifically relates to the business of insurance. . . ."

essary, liquidation (§§ 7405-7406). In these instances, the Superintendent as liquidator steps into the shoes of the insurer and, pursuant to statutory guidelines and court supervision, undertakes to perform and enforce the insolvent company's insurance contracts. The activities of the Superintendent as liquidator implement state policy governing the "relationship between insurer and insured," and the "reliability, interpretation and enforcement" of insurance policies which, as this Court has ruled, is the "core of the 'business of insurance.' " *Securities and Exchange Commission* v. *National Securities, Inc.*, 393 U.S. 453, 460 (1969).

These provisions of New York's insurance code were "adopted pursuant to" the McCarran-Ferguson Act, *Levy* v. *Lewis*, 635 F.2d 960, 963 (2d Cir. 1980). They embody a single, integrated scheme in which liquidation and distribution is a last stage of regulation in the public interest. "The business of insurance is affected with a public interest, and the state has an important and vital interest in the liquidation or reorganization of such a business." 19A J. & J. Appleman, *Insurance Law and Practice*, § 10621, at 4 (1982) (footnote omitted).

In *Law Enforcement Insurance Co.* v. *Corcoran*, 807 F.2d 38 (2d Cir. 1986), *cert. denied*, 107 S.Ct. 1896 (1987), the Court of Appeals for the Second Circuit recognized that New York's "comprehensive plan of regulation of insurance companies, with particularly detailed provisions concerning their rehabilitation and liquidation" constituted legislation "on *a matter of special state concern—so declared by the federal McCarran-Ferguson Act*, 15 U.S.C. §§ 1011-1015." 807 F.2d at 43 (emphasis added; footnote omitted).

In *Levy* v. *Lewis*, *supra*, the Circuit Court stated:

> "New York State has a complex administrative and judicial system for *regulating and liquidating* domestic insurance companies. . . .
>
> "It is also highly significant that the state scheme has been adopted pursuant to congressional authorization. In the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015,

> Congress mandated that regulation of the insurance industry be left to the individual states. Thus, *the administrative and judicial scheme erected by New York to regulate insurance companies, including that part enabling the institution and implementation of liquidation proceedings, operates pursuant to an express federal policy of noninterference in insurance matters.*" 635 F.2d at 963 (emphasis added).

Levy v. *Lewis* and *Law Enforcement Insurance Co.* v. *Corcoran* were actions asserting federal court jurisdiction of claims against insolvent insurance companies in liquidation. Both cases challenged the exclusive jurisdiction of the state liquidation court. The Second Circuit ruled that the federal courts should abstain from exercising jurisdiction in deference to the primacy of the state insurance insolvency system. *Levy* v. *Lewis*, *supra*, 635 F.2d at 963-67; *Law Enforcement Insurance Co.* v. *Corcoran*, *supra*, 807 F.2d at 43-44.

In *Washburn* v. *Corcoran*, 643 F.Supp. 554 (S.D.N.Y. 1986), the plaintiff sought an order under the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.* (1982), requiring amicus as liquidator to submit a dispute to arbitration. Requiring arbitration would have been contrary to New York law, under which the state liquidation court has exclusive jurisdiction of disputes concerning the liquidation. 643 F.Supp. at 556-57. The federal District Court for the Southern District of New York, following *Levy* v. *Lewis*, *supra*, held that New York's insurance liquidation statute is a state law "*protecting or regulating the relationship between the insurance company and the policyholder,*" and thus is a " '*law[ ] regulating the business of insurance*' " entitled to deference under the McCarran-Ferguson Act. 643 F. Supp. at 556 (emphasis added). The court accordingly held that the Arbitration Act, as a federal statute of general application, must give way under the McCarran-Ferguson Act to New York's insurance insolvency statute. Thus, arbitration could not be compelled where New York's insurance insolvency statute forbade it.

These cases show the view taken of insurance insolvency proceedings by federal courts of the Second Circuit—which is radically different from the view of the Fourth Circuit. They also illustrate the wide range of issues affected by the Fourth Circuit ruling in the case at bar, and the importance of the issue to the Superintendent as liquidator, to the policyholders of New York insurance companies of which he is the guardian, and to receivers and policyholders of insolvent insurance companies chartered in other states. The narrow issue presented by the case, the availability of a first priority for claims asserted by the federal Government, itself is of first importance, bearing as it does on the many insolvent companies owing such debts. In addition to imposing the federal priority statute on state insurance company liquidation, the circuit court decision below endangers the integrity of the entire insurance company insolvency process, as administered throughout the several states pursuant to the Uniform Insurance Liquidation Act and other similar laws. If, as the circuit court held, state insurance company liquidation is not protected by the McCarran-Ferguson Act, crucial components of the system for insurance company liquidation will be at risk of being superseded by federal statutes of general application, with unpredictable results for policyholders and others whose rights are protected by that system.

Congress has chosen, by the McCarran-Ferguson Act, to leave the regulation of insurance to the states, and the states, including the State of New York, have in response enacted detailed codes of insurance regulation, including liquidation provisions. The state insurance insolvency system protects the interests of policyholders. State laws that protect policyholders of an insolvent insurance company clearly regulate the "business of insurance", as expressly recognized by the Second Circuit. The Fourth Circuit's ruling in the case at bar creates a conflict with those rulings and raises a question which requires resolution by the United States Supreme Court.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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versus

UNITED STATES DEPARTMENT OF THE TREASURY; W.E. DOUGLAS, COMMISSIONER, UNITED STATES DEPARTMENT OF THE TREASURY, FISCAL SERVICE,
Respondents.

BRIEF OF AMICUS CURIAE STATE OF MARYLAND, *EX REL.* INSURANCE COMMISSIONER OF THE STATE OF MARYLAND IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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INTEREST OF AMICUS CURIAE, THE STATE OF MARYLAND

Amicus Curiae, the State of Maryland, on behalf of the Insurance Commissioner of the State of Maryland ("Insurance Commissioner") urges this Court to issue a writ of certiorari to review the Opinion of the United States Court of Appeals for the Fourth Circuit, 846 F.2d 272 (1988), in order to decide an issue of great public importance.

The ultimate issue to be decided in this action is whether the Federal "super-priority" statute, 31 U.S.C. §3713[1] preempts the ability of the Receiver of Eastern Indemnity Company of Maryland ("EICOM")[2] to apply the insurance laws of Maryland when conducting the company's business. The Federal statute requires payment to the Government of all amounts owed, on a dollar-for-dollar basis, regardless of any preexisting priority system, and places personal liability upon the receiver/liquidator who fails to obey its mandate. Maryland's Insurance Code, on the other hand, sets out a detailed system to pro-rate the claims against the insolvent carrier, with the aim of ensuring at least partial payment of valid claims against an insolvent insurer. *See*, Maryland Code, Ann., Article 48A, §158A, which provides that claims by "policyholders, beneficiaries, and insureds" have priority over "all other claims except for those expenses of administration, wages . . . and taxes." It is important to note that the claims upon which the Government seeks to assert a priority are merely policyholder claims, similar to all other policyholder claims nationwide, arising out of EICOM's business of surety bond underwriting. The Maryland Code pro-

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[1] This statute provides that a claim of the United States "should be paid first" in the case of an insolvent debtor. The statute further provides that "(a) representative of a person. . . paying any part of a debt. . . before paying a claim of the government is liable to the extent of the payment for unpaid claims of the Government." 31 U.S.C. §3713(b).

[2] EICOM is a Maryland domiciled surety company which was placed into receivership, followed by liquidation, by State court order beginning in 1985, pursuant to Maryland Code, Ann., Article 48A, §§132, *et seq.*

vides that tax claims of the Government are paid up front.

The Petitioner, as Receiver and liquidator of EICOM, wishes to ensure at least partial payment to all policyholders or beneficiary claimants. The Federal Government, however, asserts that the super-priority statute gives it the right to push ahead of all other claimants in seeking repayment from EICOM's meager assets. The Receiver claims that the McCarran-Ferguson Act, 15 U.S.C. §1011 *et seq.*,[3] prohibits the Government's attempt to deny all other claimants access to these assets.

In determining whether the Federal statute should be permitted to disrupt the state-mandated priority of payment scheme, the issue has narrowed to the question whether an insurance company receiver, who takes the insurer's "property and business in his own name . . . or in the name of the insurer",[4] is involved in the "business of insurance", so as to be afforded McCarran-Ferguson Act protection.

The Insurance Commissioner of the State of Maryland is the agency official charged in the first instance with conducting the business of troubled insurers in

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[3] The relevant section of this Act states:

(a) The business of insurance and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance. . .

[4] *See*, Maryland Code, Ann., Article 48A, Section 142.

this State.[5] She therefore has a preeminent interest in the outcome of this litigation, as it will affect not only the conduct of this liquidation, but all future liquidations conducted in Maryland.

Indeed, for more than a hundred years, the regulation of the insurance industry has been the exclusive right and responsibility of the several States. The federal role, both by operation of the McCarran-Ferguson Act and by case law, *Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 19 L.Ed. 357 (1869); *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408 (1946) has been abrogated to the States. This is in recognition of the fact that the insurance industry cannot respond to the needs of policyholders if regulated on a national basis, subject to all federal laws. 15 U.S.C. §1011.

Maryland, like all 50 states, extensively regulates the insurance business conducted within its borders. This regulation extends from the creation of an insurance company, through its operational life, to its termination. As a result, the citizens of Maryland look to the Insurance Commissioner to protect their interests at all stages of an insurer's operation, and to ensure that they receive the insurance protection for which they contracted. The Fourth Circuit decision in this case, if allowed to stand, would eviscerate the Maryland Insurance Commissioner's authority to carry out this public service.

The Insurance Commissioner further believes that a ruling by this Court that the Department of the

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[5] *See*, Maryland Code, Ann., Article 48A, Section 145, which provides in part that upon appointment as receiver, the Commissioner shall "immediately proceed to conduct the business of the insurer" §145(5).

Treasury is entitled to avoid the mandates of the McCarran-Ferguson Act will have a detrimental impact not only upon her ability to conduct liquidations, but also upon her overall regulatory authority.

CONSENT OF THE PARTIES

Pursuant to Rules of the Supreme Court, Rule 36.4, Amicus Curiae State of Maryland is not required to obtain written consent of the parties prior to filing a brief *amicus curiae*, in that it is a State, sponsored by its Attorney General.

ARGUMENT

I. THE INTERPRETATION GIVEN TO THE PHRASE "BUSINESS OF INSURANCE" BY THE FOURTH CIRCUIT WILL SEVERELY IMPAIR OR PROHIBIT THE REGULATION OF INSURANCE BY THE INSURANCE COMMISSIONER

The lower court, in a *per curiam* opinion, held that the McCarran-Ferguson Act is inapplicable to the activities of an insurance company receivership. *Gordon v. U.S. Treasury*, 846 F.2d 272 (4th Cir. 1988). This conclusion was based upon the underlying finding that receivership business does not fall within the McCarran-Ferguson definition of the "business of insurance" as set out in *Union Labor Life Insurance Company v. Pireno*, 458 U.S. 119 (1982), involving an interpretation of the antitrust exemption built into the McCarran-Ferguson Act. *See* 15 U.S.C. §1012(b). The effect of this decision upon the overall regulatory authority of the Insurance Commissioner is grave and holds such far-reaching consequences to the citizens of this and all other states as to warrant review by this Court.

The Maryland Insurance Code, contained in Article 48A[6] of the Maryland Code, sets up a highly complex, intricate system by which the Insurance Commissioner may regulate the insurance industry in this State. The Commissioner oversees the creation of Maryland insurers, Md. Code Ann., Corporations and Associations, Section 6-501, *et seq.*; the financial viability of these companies, §§47-50; the entrance of unauthorized insurers into the Maryland market, §§201-211A; the manner in which companies set rates, §242; the policies they use, §242(d); the risks they choose to underwrite, §234A; and how they may cancel existing risks §240AA, §234B, §240A. The Commissioner is vested with the power to ensure that valid claims are paid on a timely basis. The Commissioner regulates the manner of advertising and solicitation used by insurers, §§212, 217-219, 221; the names a company may use, §234; and myriad other functions, with the sole aim of protecting the insurance-buying public.

An unthinking application of the *Pireno* test in all circumstances would destroy not only the Commissioner's power to ensure that policyholders receive claims payment in a liquidation, but could potentially affect all aspects of her regulatory authority which are of any consequence. The lower court reasoned that, for an activity to be the "business of insurance", it must directly involve the transfer or spreading of risk, and the contractual relationship between an insurer and its insured. This, in effect, limits the scope of the "business of insurance" to the narrow param-

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[6] Unless otherwise specified, all references to the Maryland Code hereinafter shall be to Article 48A.

eters of the "business of contracting." It overlooks the fact that crucial regulatory activities, such as the review and approval of policy forms, have no direct effect upon the *actual* transfer or spread of risk among discrete individuals or the contractual relationship between the insurer and insured. Rather, this is a function involving only the Insurance Commissioner and the insurer. Similarly, Maryland's "Unfair Trade Practices Act" governs the payment of claims, false and deceptive advertising, policy cancellations, nonrenewal procedures, and coerced sales, among other things.

Under the lower court's analysis these consumer protections are not a part of "the business of insurance" because the actual "transfer" of risk occurred at the time of contracting. Yet, pursuant to this rationale, the federal government would be able to preempt the Commissioner's regulatory authority at any time. This is precisely the situation which existed in *Federal Trade Commission v. National Casualty Company*, 357 U.S. 560, where federal authorities attempted to step into various insurance commissioners' shoes, and regulate insurance company advertising. This Court refused to permit this federal intrusion, reasoning that regulatory responsibility had been delegated to the States pursuant to the McCarran-Ferguson Act, and that the States were best equipped to carry out this function.

The Insurance Commissioner does not believe the Government intends to argue that she loses her sovereign authority to regulate the insurance industry and its practices once an individual insurance contract has been signed. Yet, by limiting the definition of the "business of insurance" to only those discrete acts *by*

an insurer which actually transfer or spread risk, the Government has placed the entire regulatory structure of the insurance industry in jeopardy. Only this Court can resolve the ambiguity resulting from the lower court's decision.

The Commissioner's authority to take action in the event a company falls into financial difficulties is jeopardized by the Court of Appeals' decision. By removing the liquidation process from the aegis of McCarran-Ferguson protection, the lower court has drawn an artificial line through the insurance regulatory process, leading to untenable and illogical results which only review by this Court can correct.

Both the Government and the lower court have taken a dangerously myopic view of the liquidation process. It is neither logical, nor practical, to view liquidation in a vacuum. Rather, liquidation is merely the continuation, albeit to termination, of an ongoing business, and is merely the final stage in the lifecycle of an insurance company. The Maryland Insurance Code recognizes that this stage necessarily involves the continuation of the "business of insurance." When an order of rehabilitation is issued, pursuant to §141, the order "shall direct the Commissioner forthwith to take possession of the property of the insurer *and to conduct the business thereof*. . . ." (emphasis supplied). Liquidation is merely the next step. It is logically inconsistent to assert that a company under the control of the Commissioner during rehabilitation is afforded McCarran-Ferguson protection, but that a company in the process of concluding its affairs and paying policyholder claims is not. Yet, the claim that the "business of insurance" does not en-

compass the adjustment and payment of claims by a company in liquidation draws just this arbitrary line, and effectively removes the Commissioner's ability to protect her citizens at precisely the time it is most important that she do so. When the insurance industry, or any of its members is in financial difficulty, it is imperative that the various insurance commissioners retain their regulatory authority. It is precisely in circumstances such as EICOM's that the potential for policyholder injury is greatest.

The consequences of the Fourth Circuit's interpretation are grave. Insurance companies frequently operate in many states.[7] By defining the rehabilitation/liquidation process as outside the "business of insurance", and hence, outside McCarran-Ferguson protection, the lower court creates insurmountable problems for the conduct of receiverships nationwide. If the Fourth Circuit is correct, and receiverships are not the "business of insurance", the several states are robbed of their ability to protect and preserve assets for the benefit of policyholders, by the potential intrusion of overriding and conflicting federal laws and regulations. Yet, there is no other overall scheme to fill the void and ensure this protection. Congress, in recognition of this fact, has declared that the states must be afforded the preeminent right to conduct insurer insolvencies. *Baldwin-United Corp. v. Garner*, 678 S.W. 2d 754 (Ark. 1984). The reasoning of the *Baldwin-United* court, which is in direct conflict with the lower court's decision here, is particularly relevant. It is also particularly illustrative of the unten-

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[7] In Maryland, for example, as of December 31, 1987, 1,291 companies were licensed to do business. Of these, only 56 are domiciled in this State.

able ramifications which would result should the lower court's decision be left unreviewed. In *Baldwin-United*, the parent company of three insolvent Arkansas insurers brought suit in federal court to set aside the rehabilitation plans created for those insurers by the State-run receivership. The Court refused, reasoning that insurance company liquidation intimately involves the relationship between the insurer and its insureds and is, therefore, the "business of insurance" intended to be protected by McCarran-Ferguson:

> The Plan of Rehabilitation protects over 300,000 policyholders throughout the United States by attempting to provide the Arkansas insurance companies with assets at least sufficient to support the full amount of the accumulated value of the annuities.

Baldwin-United v. Garne 678 S.W.2d at 758. As a result, the assets of the insurers were not within reach of the parent corporation, and were available to the State for the benefit of policyholders.

The Arkansas court recognized that the activities of a receiver, including payment of claims and gathering assets with which to pay the claims, is at the very heart of the relationship between a policyholder and its insurer, and is an integral part of the regulatory scheme preserved to the states by McCarran-Ferguson. *See, also, Washburn v. Corcoran*, 643 F. Supp. 554 (SDNY 1986); *Idaho v. IRS*, 662 F. Supp. 60 (D. Idaho 1987), *reversed and remanded*, No. 87-4057 ___F.2d ___(9th Cir). Removing McCarran-Ferguson protection would open the door to actions such as the one contemplated in *Baldwin-United*. Without

clarification by this Court, the scope of the Commissioner's power to fulfill the contractual obligations of an insolvent insurer is in serious doubt.

II. THE INTERPRETATION GIVEN TO THE PHRASE "BUSINESS OF INSURANCE" BY THE FOURTH CIRCUIT IS IN DIRECT CONFLICT WITH PRIOR INTERPRETATIONS BY THIS COURT

In concluding that the settlement and payment of claims by EICOM's liquidator is not the "business of insurance", the District Court and, by adoption, the Court of Appeals, applied a three prong "test" set out by this Court in *Union Labor Life Insurance Company v. Pireno*, 458 U.S. 119 (1982). In doing so, the lower court ignored the fact that the *Pireno* Court was construing the "business of insurance" provision in the context of its narrow antitrust exception. The court failed entirely to address and reconcile *Pireno* with this Court's earlier decision in *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453 (1969). This misinterpretation will have grave consequences upon insurance commissioners' ability to regulate the insurance industry in their various states. Only review by this Court can resolve this conflict.

The *Pireno* case, in the antitrust context, held that three questions must be answered in the affirmative in order for certain activities to constitute the "business of insurance":

> 1. Does the activity in question relate to the 'spreading and underwriting of a policyholder's risk'? 458 U.S. at 127.
>
> 2. Does the activity in question relate to the contract between the insurer and the insured? 458 U.S. at 128.

> 3. Is the activity in question limited to entities within the insurance industry? 458 U.S. at 129.

In blindly applying these three criteria outside the context of antitrust actions, the lower courts ignored, and thereby nullified, the effect of this Court's reasoning in *National Securities* (involving the SEC's attempt to regulate the merger of two insurers). In that case the Court concluded that the relationship between the insurers and their shareholders was not the "business of insurance," and hence not subject to McCarran-Ferguson protection. The Court reasoned that the relationship of primary importance in the regulatory scheme is the relationship between the insurer and insured. Statutes whose purpose it is to regulate this relationship "directly or indirectly" are preserved from federal intervention by the operation of the McCarran-Ferguson Act. In this way, Congress ensured continued state sovereignty in regulating the insurance industry, and activities which have no nexus to insurance may be regulated by the appropriate entity, federal or state. The Insurance Commissioner believes there is nothing more intimately connected to the relationship between an insurer and insured than the orderly and fair payment of claims.

In holding that the "business of insurance" ceases once a contract of insurance has been signed the lower court also ignored the earlier case of *Federal Trade Commission v. National Casualty Company*, 357 U.S. 560 (1958), which held that advertising by insurance companies is properly left to state regulation, pursuant to McCarran-Ferguson.

If this Court fails to clarify the scope of the phrase "business of insurance", serious questions will arise

concerning the proper interpretation to be afforded to both the *SEC v. National Securities, supra* and *FTC v. National Casualty, supra* decisions.

Indeed, the lower court's decision calls into question the very language of the McCarran-Ferguson Act itself. The lower court definition of the phrase "business of insurance" renders not only the prior decisions of this Court meaningless, but also the language of Section 1014 of the Act.[8] An interpretation of a statute which renders its plain language meaningless or absurd is an incorrect interpretation. *Mountain States Telephone and Telegraph Company v. Pueblo of Santa Ana*, 105 S.Ct. 2586, 2594 (1985); *Colautti v. Franklin*, 99 S.Ct. 675, 684 (1979). Yet neither the Government nor the lower court addressed or reconciled the effect of their interpretation of the phrase "business of insurance" upon this Court's prior pronouncements and on the statute itself.

CONCLUSION

The insurance industry is one of the most highly regulated industries in this country. This pervasive scheme of regulation, encompassing the birth, growth and death of insurance companies, has as its underlying purpose the protection of millions of policyholders and beneficiaries nationwide. Congress, through the McCarran-Ferguson Act, placed the responsibility

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[8]This section states: "Nothing contained in this chapter shall be construed to affect in any manner the application to the business of insurance of the Act of July 5, 1935 . . . known as the National Labor Relations Act, or the Act of June 25, 1938, as amended, known as the Fair Labor Standards Act of 1938 . . ."

to regulate this industry within the jurisdiction of the several states. The lower court decision casts long-reaching shadows over the ability of the states to carry out this mandate, and places in doubt decisions of this Court and of other courts which have faced this question. It is imperative that Maryland's ability to protect its citizens be preserved and that this Court clarify the scope of its sovereign authority to do so. For these and the foregoing reasons, the State of Maryland as *amicus curiae* respectfully prays that the Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, *et al.*,

Respondents.

AMICI CURIAE BRIEF OF THE PROPERTY AND CASUALTY INSURANCE GUARANTY CORPORATION, THE ILLINOIS INSURANCE GUARANTY FUND, THE WISCONSIN INSURANCE SECURITY FUND AND JAMES T. ODIORNE IN HIS CAPACITY AS TEXAS ANCILLARY RECEIVER FOR EASTERN INDEMNITY COMPANY OF MARYLAND

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IV.

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The Amici Curiae respectfully pray that James A. Gordon's petition that a writ of certiorari issue to review the opinion of the United States Court of Appeals for the Fourth Circuit be granted.

CONSENT

Pursuant to United States Supreme Court Rule 36.1, a copy of the written consent of the Parties to the filing of this Amici Curiae Brief on behalf of The Property and

Casualty Insurance Guarantee Corporation, the Illinois Insurance Guaranty Fund, the Wisconsin Insurance Security Fund, and James T. Odiorne in his capacity as Texas Ancillary Receiver for Eastern Indemnity Company of Maryland, is separately enclosed.

STATEMENT OF THE CASE

The Petitioner asks this Court to decide a critical issue under the McCarran-Ferguson Act and to thereby resolve a conflict between:

(1) The Maryland insurer liquidation statute which requires a liquidator to pay claims of policyholders in full prior to paying other creditors' claims (MD. ANN. CODE art. 48A, § 132 *et seq.* (1986)); and

(2) A federal statute first enacted in 1797 which provides that a claim of the United States shall be paid first when a person indebted to the government is insolvent (31 U.S.C.A. § 3713 (West Supp. 1988)).

The McCarran-Ferguson Act, 15 U.S.C.A. § 1011 *et seq.* (West 1976), provides that the business of insurance shall be regulated by the states and that "[n]o Act of Congress shall be construed to invalidate, impair or supersede any [state] law . . . regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." The McCarran-Ferguson Act thus mandates that conflicts be resolved in favor of state laws regulating the "business of insurance" absent specific application of federal law to the insurance business. Nevertheless, the District Court ruled in favor of the general federal priority statute, reasoning that the Maryland statute governing insur-

ance company insolvency and liquidation proceedings was not a law enacted for the purpose of regulating the "business of insurance" as that term is defined under the McCarran-Ferguson Act. The United States Court of Appeals for the Fourth Circuit affirmed the District Court's decision, adopting the lower court's opinion as its own.

STATE INSURANCE GUARANTY ASSOCIATIONS' INTEREST IN THE DISPUTE

All fifty states and the District of Columbia have enacted statutes establishing insurance guaranty associations. An insurance guaranty association is a non-profit association of all of the property and casualty insurers licensed in a particular state. An insurance guaranty association's purpose, subject to certain limitations, is to pay the residents of its state who have claims under insurance policies issued by insolvent insurers that were licensed to do business in that state. Upon paying such claims, a guaranty association receives a claim in the insolvent insurer's liquidation proceedings equal to the amount of the claims paid. If the guaranty association is unable to satisfy its claim against the insolvent insurer's estate (in whole or in part), it assesses its member companies by the amount of the short fall and the member companies, in turn, raise their policyholder's premiums to recoup the cost of this assessment. The federal government's assertion that it has a "super-priority" over the claims of other policyholders and the guaranty associations will, therefore, have a substantial impact, not only on the final resolution of Eastern Indemnity's insolvency, but on the liquidation procedures of all fifty-one U.S. guaranty associations.

If the Fourth Circuit opinion is allowed to stand, the decision will adversely affect state insurance liquidation proceedings and diminish policyholder protection in at least two respects:

First, the federal government's asserted priority will cause policyholders of insolvent companies to suffer a lower priority claim with respect to claims not covered by state guaranty associations. All state guaranty associations place limits on the claim amounts subject to guaranty association protection. Some associations may also not cover certain lines of business (such as surety bonds).[1] Claims in excess of guaranty association limits or claims in excluded lines of business can only be collected from the estate of the insolvent insurer.

Second, all state guaranty associations have annual limits on the maximum assessments that may be levied against member companies to pay covered claims. If the federal "super-priority" is upheld, more of the insolvent insurers obligations will be borne by guaranty associations which, in turn, will lower the capacity of the associations to respond to insolvencies. Moreover, the decision will require insurance policyholders generally to bear the added burden of the federal "super-priority."

The Property and Casualty Insurance Guarantee Corporation (the "Maryland Guaranty Corporation") is the in-

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[1] *See* TEX. REV. CIV. STAT. ANN. art. 21.28-C § 1 (Vernon 1987) (surety bonds excluded from the scope of the Texas Property and Casualty Guaranty Association's protection). Other states, including Illinois, have recently amended their guaranty fund statutes to exclude surety bonds. *See* ILL. ANN. STAT. ch. 73, § 1065.83(c) (Smith-Hurd Supp. 1988).

surance guaranty association created under Maryland law.[2] The Illinois Insurance Guaranty Fund (the "Illinois Fund") is the insurance guaranty association created under Illinois law.[3] The Wisconsin Insurance Security Fund (the "Wisconsin Fund") is the insurance guaranty association created under Wisconsin law.[4] The Maryland Guaranty Corporation and the Illinois fund are two of the eight state insurance guaranty associations that will pay claims under surety bonds issued by Eastern Indemnity.[5] The guaranty associations in the other twenty-six states where Eastern Indemnity was licensed provide no coverage at all for claims under surety bonds. Non-governmental bondholders in those states must collect from the estate of the insolvent insurer, or not at all.

Section 158A of the Maryland Insurance Code, like almost all state insurance liquidation statutes, gives guaranty association claims and policyholder claims that are not covered by guaranty associations equal priority. If the Fourth Circuit's decision is allowed to stand, payment of the government's claim will completely exhaust the Eastern Indemnity estate. There will be no assets left to pay the claims of the eight guaranty associations burdened by Eastern Indemnity's insolvency. Moreover, if the government's "super-priority" is allowed, policyholder claims in the twenty-six states where Eastern Indemnity did business and whose guaranty funds do not cover surety bonds will be rendered worthless.

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[2] MD. ANN. CODE art. 48A, § 504 *et seq.* (1986).

[3] ILL. ANN. STAT. ch. 73, § 1065.82 *et seq.* (Smith-Hurd Supp. 1988).

[4] WIS. STAT. ANN. § 646.01 (West Supp. 1986).

[5] The other guaranty associations that will pay claims under surety bonds issued by Eastern Indemnity are: Georgia, Nevada, Texas, Michigan, Louisiana and the District of Columbia.

Guaranty associations are not operated as state agencies and are not funded by state tax revenues. Instead, guaranty associations assess their member insurance companies for the money needed to pay claims. The assessed companies, in turn, recoup the amount of those assessments by charging their policyholders higher premiums. Section 516 of the Maryland Insurance Code, for example, requires members of the Maryland Guaranty Corporation to include in their premiums amounts sufficient to recoup any assessments by that Guarantee association. Similarly, the Illinois courts have expressly recognized that through their premiums, policyholders of solvent companies pay for the Illinois Fund's coverage of the policyholders of insolvent Illinois insurers. *Adams v. The Illinois Insurance Guaranty Fund*, 85 Ill. App. 3d 867, 869, 407 N.E.2d 638, 640 (1980).

To the extent that guaranty associations recover on their claims against insolvent companies, they return those amounts to their members who, in turn, reduce their policyholder's premiums.[6] Everytime a policyholder pays his or her premium to a licensed, *i.e.*, member, company, part of that premium goes to pay the claims of policyholders of insolvent insurers. Therefore, the less a guaranty association is able to recover from the estate of an insolvent insurer, the greater the burden it must place on the policyholders of its members.

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[6] *See* MD. ANN. CODE art. 48A, § 516 (1986):

> The rates and premiums charged for insurance policies and surety bonds . . . shall include amounts sufficient to recoup . . . a sum equal to the amounts paid to the Corporation by the member insurer *less any amounts returned to the member insurer by the Corporation*. . . .

(emphasis added).

If the decision of the Fourth Circuit Court of Appeals is allowed to stand, there will be no assets left to reimburse the eight guaranty associations burdened by Eastern Indemnity's insolvency, and those guaranty associations will be forced to pass on the cost of the claims they cover to the policyholders of their member insurers.

The long-term effect of that decision will be borne by the insurance buying public and as the primary function of this country's guaranty associations is the protection of the insurance buying public, the Amici guaranty associations have a very real interest in seeking this Court's review of the Circuit Court's decision.[7]

TEXAS ANCILLARY RECEIVER'S INTEREST IN THE DISPUTE

James T. Odiorne is the Texas Ancillary Receiver for Eastern Indemnity. Pursuant to the order appointing him ancillary receiver and pursuant to Article 21.28 of the Texas Insurance Code, Mr. Odiorne has taken possession of certain Eastern Indemnity assets located in the State

[7] *See* MD. ANN. CODE art. 48A, § 504(a)(1) (1986):

> The purposes of this subtitle are to provide a mechanism for the prompt payment of covered claims under certain insurance policies and to avoid financial loss to residents of Maryland who are claimants or policyholders of an insurer, *including surety*, which has become insolvent; and to provide for the assessment of the cost of such payments and protection among insurers.

(emphasis added). *See also* WIS. STAT. ANN. § 646.01(2)(a) (West Supp. 1986). *And see* ILL. ANN. STAT. ch. 73, § 1065.82 (Smith-Hurd Supp. 1988).

of Texas. Mr. Odiorne has the right and duty to use those assets to determine and pay the claims of Eastern Indemnity's Texas policyholders as well as those of the Texas Property and Casualty Insurance Guaranty Association (the "Texas Guaranty Association"). While Mr. Odiorne has the right to use Eastern Indemnity's Texas assets to pay the expenses of the receivership's administration, the Fourth Circuit's decision has effectively exhausted those assets and the costs of the receivership are being covered by the Texas Guaranty Association.

The Fourth Circuit's decision stripped Mr. Odiorne of the assets he was supposed to use to carry out his statutory duty of protecting Texas policyholders. The Circuit Court's holding has left the Texas Ancillary Receiver with insufficient assets to pay the administrative expenses of determining policyholder claims, let alone the assets needed to actually pay those claims. While the Texas Guaranty Fund has "taken up the slack" somewhat, assessing its members to cover the costs of the federal government's asserted claim, the ultimate cost of the Texas Guaranty Fund's rescue will be borne by Texas consumers.

Thus, because of his immediate concern regarding the costs and consequences of Eastern Indemnity's liquidation and his overall concern regarding the potential impact of the Fourth Circuit's decision on future Texas receiverships, the Texas Ancillary receiver has a very real interest in seeking this Court's review of the lower court's decision in this case.

SUMMARY OF ARGUMENT AND REASONS FOR GRANTING THE WRIT

The Maryland Liquidator and these Amici Curiae take the position that the McCarran-Ferguson Act, 15 U.S.C.A. § 1011 *et seq.* (West 1976), both by its express language and its intended purpose, negates the government's "all mine" contention and renders the general provisions of 31 U.S.C.A. § 3713 (West Supp. 1988) inapplicable to this case. The relevant provisions of the McCarran-Ferguson Act are as follows:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (b) *No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance,* or which imposes a fee or tax upon such business, *unless such Act specifically relates to the business of insurance*: Provided, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

15 U.S.C.A. § 1012 (West 1976) (emphasis added).

By holding that the liquidation of an insolvent insurance company does not fall within the McCarran-Ferguson Act's definition of the "business of insurance," the Fourth Circuit's opinion does violence to that Act's intent, purpose and express language; is unfair and inequitable to many

of those involved in government construction work; and misconstrues prior decisions of this Court interpreting that Act in its narrow anti-trust context.[8]

Moreover, a decision by this Court on the issue presented is urgently needed now because:

1) Other federal courts have held that the liquidation of an insolvent insurance company constitutes the "business of insurance" for McCarran-Ferguson Act purposes;[9]

2) The Court of Appeals decision will have a direct impact on all ongoing and future insurance company liquidations wherein the federal government is a claimant—leaving state liquidators shackled with the threat of personal liability for incurring expenses that reduce the government's take, even those expenses necessary to marshall all of the insolvent estate's assets;

3) Finally, the Court of Appeals decision threatens more than the liquidation process. The Fourth Circuit's holding that the regulation of such a central aspect of the insurance industry does not constitute the regulation of the "business of insurance" for McCarran-Ferguson Act purposes, calls into question many of the most funda-

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[8] *See* James A. Gordon's Petition for Certiorari in this matter, p.8 n.5 (citing: *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982); *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979) and *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453 (1969)) (hereinafter "Gordon Petition").

[9] *See* Gordon Petition, p.8 n.5 (citing: *Washburn v. Corcoran*, 643 F.Supp. 554 (S.D.N.Y. 1986) and *Idaho ex rel. Soward v. Internal Revenue Service*, 662 F.Supp. 60 (D. Idaho 1987)). Although the latter was recently overturned by the United States Court of Appeals for the Ninth Circuit, that fact merely underscores the need for this Court to review and settle this issue once and for all. *See* 88 Daily Journal D.A.R. 11528 (September 9, 1988).

mental aspects of state insurance regulation and gives the federal government the means to sidestep the McCarran-Ferguson Act in numerous other insurance regulatory contexts. Armed with the Circuit Court's decision, the government will be able to challenge any state insurance law it finds objectionable, establishing in the courts that which to date has been denied by Congress—a federal body of insurance law.

ARGUMENT AND REASONS FOR GRANTING THE WRIT

I.

THIS COURT SHOULD DECIDE WHETHER THE "BUSINESS OF INSURANCE" UNDER THE McCARRAN-FERGUSON ACT IS LIMITED TO THE BUSINESS OF SOLVENT INSURANCE COMPANIES.

The essence of the Fourth Circuit's decision is that the McCarran-Ferguson Act applies only to the regulation of solvent insurance companies. However, neither the McCarran-Ferguson Act itself, common sense, public policy or case law support such a result.

The Maryland Insurance Code's liquidation provisions are part of the overall statutory scheme by which Maryland regulates the business of its insurers. Like every state, Maryland keeps a close watch on its insurance industry—from formation and licensing (MD. ANN. CODE art. 48A, § 42 *et seq.* (1986)) to dealings with policyholders (MD. ANN. CODE art. 48A, §§ 375, 242 (1988)) to the cancellation of policies (MD. ANN. CODE art. 48A, § 240A (1988))

to the rehabilitation and liquidation of insolvent companies, MD. ANN. CODE art. 48A, § 141 (1986).[10]

Subtitle 10 of the Maryland Insurance Code, which governs insolvency and liquidation proceedings against insurers, and section 158A of that subtitle, which gives policyholders priority in the distribution of an insolvent insurer's assets, regulate the "business of insurance" at its most basic and fundamental level, namely paying the claims of policyholders. By governing what this Court has held to be the core of the "business of insurance"—the relationship between an insurer and its policyholders, *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453, 460 (1969), the Maryland liquidation priority statute regulates the very essence of that state's insurance industry.

The mere fact that a liquidator replaces the board of directors of an insurance company should not alter the basic nature of the insurer/insured relationship. If, it does and the McCarran-Ferguson Act applies only to the regulation of solvent companies, that is a far-reaching decision that only this Court should make.

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[10] *See* WIS. STAT. ANN. § 645.01(4)(f) (West 1980) ("The purpose of this chapter is the protection of the interests of insureds, creditors, and the public generally, . . . through . . . *[r]egulation of the insurance business* . . . .") (emphasis added).

II.

THE COURT OF APPEALS DECISION WILL UNFAIRLY DEPRIVE MANY WHO WORK ON GOVERNMENT PROJECTS OF ANY MEANS OF FINANCIAL PROTECTION.

Like most states, Maryland gives the policyholders of an insolvent insurer a priority over all other claimants (with the exception of the liquidator, certain employees, and state and federal tax authorities). MD. ANN. CODE art. 48A, § 158A (1986). Courts which have interpreted similar provisions in other jurisdictions have recognized that this type of priority protects the interests of the insurance buying public—those who most need protecting when an insurer becomes insolvent. *American Re-Insurance, et al. v. Washburn, et al.*, 122 Ill. 2d 555, 566-68, 524 N.E.2d 538, 542-43 (1988). The Fourth Circuit's decision, however, completely ignored this interest and stripped Eastern Indemnity's non-governmental bondholders of the protection they had contracted for and, in many cases, of their state law lien rights as well.

Maryland's priority statute requires *all* of Eastern Indemnity's policyholders to share pro rata in the liquidated assets of that company in accordance with the cardinal rule of liquidation—no member of a class of creditors shall be allowed a preference over the other members of that same class.[11] By thwarting this distribution scheme, the

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[11] *See People v. Cosmopolitan Insurance Company*, 89 Ill. App. 2d 225, 223 N.E.2d 90 (1987):

> The insolvency of an insurance company casts burdens upon its insureds, claimants against its insureds and, if a stock company, against its stockholders. The consequences to those injured are severe. This court cannot, however, . . . seek to lessen the injury of one . . . at the expense of other injured persons . . . .

(Footnote continued on following page)

Fourth Circuit Court completely negated the equitable purpose of that statute and doomed hundreds of contractors, laborers, and materialmen to receive no payment at all on their claims under Eastern Indemnity's surety bonds.

Moreover, many of the claimants who will be denied recovery from the Eastern Indemnity estate are claimants under Miller Act bonds issued by Eastern Indemnity in connection with federally funded construction projects. One type of Miller Act bond is a performance bond designed to protect the government's interests as the owner of a project.[12] Another type of Miller Act bond is a payment bond designed to protect the interests of laborers and materialmen who perform services or provide goods for the benefit of a government owned project.[13] Denying recovery from the Eastern Indemnity estate under this second type of bond is particularly harsh since, under the Miller Act, these laborers and materialmen will also be denied their normal state law lien rights. Because they have no enforceable rights against the federal government and cannot acquire liens on public property, these laborers' and materialmen's only possible source of protection are the Miller Act payment bonds issued by Eastern Indemnity.[14]

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[11] *continued*

Id., at 93. *See also General Reinsurance Corp. v. Missouri General Insurance Co.*, 458 F. Supp. 1, 5 (W.D. Mo. 1977), *aff'd.* 596 F.2d 330 (8th Cir. 1978).

[12] 40 U.S.C.A. § 270a (West 1986).

[13] 40 U.S.C.A. § 270b (West 1986).

[14] *See Ramsdell v. G.H. Coffey Co., Inc.*, 632 F.2d 162, 163 (1st Cir. 1980) (ordinarily, sovereign immunity bars attachment and garnishment of government funds and an unpaid subcontractor's remedy under sections 270a to 270d of this title is a payment bond). *See also U.S. ex rel. B's Co. v. Cleveland Elec. Co. of S.C.*, 373

(Footnote continued on following page)

However, under the Circuit Court's decision, the government will be able to side-step the Maryland insurance laws that would allow these laborers and materialmen the right to share equally with the government in the Eastern Indemnity assets.

III.

MANY OTHER CURRENT INSURER INSOLVENCY PROCEEDINGS, AS WELL AS FUTURE INSOLVENCIES, WILL BE DIRECTLY IMPACTED BY THE CIRCUIT COURT'S DECISION.

The Amici Curiae ask this Court to grant the Petitioner's petition for a writ of certiorari because of the effect that the final resolution of this case will have on a number of insurer insolvency proceedings currently underway as well as on future insolvencies which will undoubtedly occur.

As stated above, Maryland, like most states, has attempted to protect the policyholders of insolvent insurers by giving them a preference in the distribution of those insurers' assets. Giving the federal government a "superpriority" over all other policyholders will disrupt these priority systems and cast doubt upon the protection such statutes actually provide non-government policyholders.

In addition, the Fourth Circuit's decision will have a chilling effect on the conduct of insurer liquidation proceedings. With the Circuit Court's decision in hand, the federal government will continue to use 31 U.S.C.A. § 3713 (West Supp. 1988) to threaten state insurance liqui-

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[14] *continued*

F.2d 585, 589 (4th Cir. 1967) (suit under 270a to 270d of this title is the only remedy for an unpaid subcontractor on a government project; he has no claim or lien against the government).

dators with personal liability if its claims are not paid first. Such threats paralyze liquidators, who fearing personal liability, are hesitant to perform their statutory duties.[15] Moreover, if the federal government's intimidation tactics continue, they will no doubt discourage qualified persons from serving as liquidators.

IV.

THE CIRCUIT COURT'S DECISION FOR THE FIRST TIME CALLS INTO QUESTION WHETHER MANY OF THE MOST FUNDAMENTAL ASPECTS OF STATE INSURANCE REGULATION COME WITHIN THE "BUSINESS OF INSURANCE".

The rationale of the Fourth Circuit's decision places many basic and fundamental aspects of regulating and conducting the business of insurance outside the scope of the McCarran-Ferguson Act's protection. To accept the Circuit Court's view that the only activities which constitute the "business of insurance" (and are thus protected) are those directly connected to underwriting and policy issuance, leads to the conclusion that statutes regulating the formation and licensing of insurers do not regulate the "business of insurance." Yet this fundamental state regulatory power is unquestionably the type of insurance regulation that Congress intended to preserve for the states when it enacted the McCarran-Ferguson Act. Indeed, this Court itself has stated that state laws regulating the licensing

[15] *See* Affidavit of Fred Nepple dated 9-13-88 (Appendix 1), regarding the federal government's attempt to sue Nepple personally for satisfaction of an Internal Revenue claim against an insolvent insurer Nepple was liquidating. *See also* letter from Harry Eakin (liquidator of Allied Fidelity Insurance Co.) dated 1-13-88 (Appendix 2), informing all state insurance guaranty funds that their claims against Allied Fidelity's estate would not be paid until the issue of the federal government's alleged priority has been resolved.

of insurers are laws regulating the "business of insurance." *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. at 460. *Cf. Robertson v. People of the State of California*, 328 U.S. 440 (1946).

Similarly, the Fourth Circuit's limited interpretation of this phrase would mean that an insurer's dealings with its policyholders (once a policy has been issued) do not constitute the "business of insurance" and that a state's unfair trade practice statutes which govern those dealings do not regulate the "business of insurance" and are not entitled to McCarran-Ferguson protection. *See* MD. ANN. CODE art. 48A, §§ 240A and 227 (1986 and 1988 respectively) (restricting an insurer's right to cancel policies after they have been written and prohibiting insurers from improperly inducing policyholders to cancel their policies).[16] Nothing in this Court's prior decisions interpreting the McCarran-Ferguson Act in its narrow anti-trust context, justifies or supports such a result.[17]

CONCLUSION

While this Court's caseload is severe, the instant case, presenting a pervasive insurance regulatory issue that will have an impact on the rights of insureds and claimants

[16] Ironically, the District Court which decided the case at bar has itself recognized that Maryland's unfair trade practice provisions regulate the "business of insurance" and are, in fact, entitled to the protection of the McCarran-Ferguson Act. *State of Maryland v. Blue Cross and Blue Shield*, 620 F. Supp. 907, 919-20 (D. Md. 1985). *See also Mathis v. Automobile Club Inter-Insurance Exchange*, 410 F. Supp. 1037, 1040 (W.D. Mo. 1976).

[17] *See supra* note 7 and accompanying text.

in all fifty states and the District of Columbia, merits this Court's review.

Respectfully submitted,

THOMAS W. JENKINS
HUGH C. GRIFFIN *
MARK R. GOODMAN
LORD, BISSELL & BROOK
115 South LaSalle Street
Chicago, Illinois 60603
(312) 443-0342

Counsel for Amici Curiae

* Counsel of Record

APPENDICES

APPENDIX 1

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1988

JAMES A. GORDON, Special Deputy State Insurance Commissioner of Maryland and Receiver for Eastern Indemnity Company of Maryland,

Petitioner,

v.

UNITED STATES DEPARTMENT OF THE TREASURY, ET AL.,

Respondents.

AFFIDAVIT

STATE OF WISCONSIN
COUNTY OF DANE—ss.

Fred Nepple, being duly sworn upon oath, deposes and says:

1. Affiant is an attorney and employee of the Office of the Commissioner of Insurance of the State of Wisconsin, and at all times pertinent hereto was personally involved in the matters set forth below.

2. In 1975 Wisconsin Surety Corporation was an insurer domiciled in Wisconsin, and was in the business of selling surety bonds.

3. In April 1975 the Office of the Commissioner of Insurance of the State of Wisconsin placed Wisconsin Surety Corporation into liquidation, under the jurisdiction of the Liquidation Court, Dane County Circuit Court, Case No. 146-166.

4. The Court appointed the Wisconsin Commissioner of Insurance as Liquidator.

5. The United States of America, Internal Revenue Service, was one of the claimants in the liquidation estate, with certain specific claims seeking recovery under the provisions of surety bonds issued by the insolvent insurer, and with other specific claims seeking other types of recovery against the insolvent insurer.

6. In May 1984 the liquidation was completed and proceedings were terminated.

7. As of the termination date, the Liquidator pursuant to Wisconsin insurance liquidation law had paid none of the claims of the United States of America seeking recovery under the surety bond provisions.

8. In February 1985 representatives of the Office of the Commissioner of Insurance for the State of Wisconsin were notified that the United States of America was considering an action against the Commissioner, and that it asserted priority for all unpaid claims under Title 31, U.S.C. § 3713, and that it asserted personal liability against the Commissioner under Title 31, U.S.C. § 3713.

9. The aggregate amount of all claims and interest sought by the United States of America was approximately $200,000.

10. The liquidation proceedings were reopened, and a settlement was reached in 1987.

11. All facts set forth above in paragraphs 1-8 and 10 are filed with the Liquidation Court as a matter of public record in such Case No. 146-166.

/s/ FRED NEPPLE

Subscribed and sworn to
before me this 13th day
of September, 1988.

/s/ _____

Notary Public, Dane County
Wisconsin
My Commission: is permanent.

STATE OF WISCONSIN
CIRCUIT COURT
DANE COUNTY

In the Matter of the Liquidation of
WISCONSIN SURETY CORPORATION,
a Wisconsin Insurance Corporation.

REPORT ON CLAIM AND ORDER
CD #425A, B & C
CD #436A, B & C
Case No. 146-166

The Liquidator hereby reports to the Court regarding the above claim.

STATEMENTS BY CLAIMANT

The undersigned, being sworn, under the cooperation and perjury provisions of the Wisconsin Statutes states that:

1. The name and address of claimant is:
   United States
   Internal Revenue Service
   U.S. Department of Justice, Tax Division
   Washington, D.C. 20530

2. On the date of the insured event or on April 11, 1975 claimant was not [strike if appropriate] a resident of the State of Wisconsin (or a corporation organized under Wisconsin law).

[3. Claimant has not [strike if appropriate and furnish all pertinent details] received or acquired a preference, lien, conveyance, transfer, assignment or encumbrance voidable under Chapter 645, Wisconsin Statutes; and claimant does not [strike if appropriate and furnish all pertinent details] *hold security relating to this matter.]**

[4. Claimant has exerted and will continue to exert every reasonable effort to minimize any loss which is the subject of this claim, and to date has not [strike if appropriate and furnish all pertinent details] *received any payment regarding such loss; and claimant immediately will report to the Liquidator any such payment received subsequent to this date.]*

5. In consideration of the recommendation of the Liquidator of Wisconsin Surety Corporation regarding payment of part or all of the claim of the claimant bearing the above court docket number, the claimant hereby for himself, his heirs, executors, administrators and assigns, (or for itself, its successors and assigns) does remise, release and forever discharge such Liquidator and the Wisconsin Commissioner of Insurance each individually and in his official capacity, his heirs, executors, administrators, assigns and successors in office, and the estate of the Wisconsin Surety Corporation, from any and all right, cause of action, claim or demand of whatsoever kind, nature or description at law or in equity or created by statute which the claimant now has or which his heirs, executors, administrators or assigns (or its successors or assigns) can, shall, or may hereafter have.

6. Claimant hereby stipulates his approval of the determination by the Liquidator as set forth herein.

/s/ JEFFREY D. SNOW
Signature of person authorized
to act for claimant

---

* Bracketed and italicized portions throughout were stricken in the original copy.

[On this ____ day of _____, 19____, before me personally appeared _____ to me personally known and known to be the same person described in and who executed the foregoing instrument and who duly acknowledged to me that he executed the same.]

On this 11th day of March, 1987, before me personally appeared Jeffrey D. Snow, to me known to be the person who executed the foregoing instrument, and to me known to be the attorney for said [Corporation], entity, and acknowledged that he executed the foregoing [as such officer as the deed of said Corporation] by its authority.

[Strike non-applicable paragraph]

(Notarization omitted in printing.)

STATEMENTS BY LIQUIDATOR

6. The claimant filed a written proof of claim which is deemed to have been timely filed in substantial compliance with Wis. Stats. §645.61 and which has received from this Court the above docket numbers.

7. The particulars of such claim and the amount claimed are as follows:

See attached.

8. The amount allowed in the determination by the Liquidator as set forth below does not exceed the amount of the bond under which this claim is made.

DETERMINATION BY LIQUIDATOR

WHEREFORE, on the basis of the foregoing and the records and data in the possession of the Liquidator and related investigation, the Liquidator hereby:

1) Recommends *[(reports)]* the allowance of the above-described claim in the amount of $28,102.33, with the amount allowed to be eligible for distribution to the claimant as follows: in Class 3 the amount of $24,128.53, *[in Class ____ the amount of $_____, in Class ____ the amount of $_____]* and in Class 5 the amount of $3,973.80, *[all pursuant to Wis. Stats. § 645-68 on a pro rata basis with all other approved claims in the above liquidation proceeding.]*

[2) Recommends the disallowance in full of the above-described claim.]

Dated: March 17th, 1987

LIQUIDATOR OF
WISCONSIN SURETY CORPORATION

By: /s/ CHRISTOPHER J. WILCOX

P.O. Address:

LaFollette, Sinykin, Anderson & Munson
Suite 300, 222 W. Washington Avenue
Madison, Wisconsin 53703

ORDER

Upon this record herein and the foregoing Report of the Liquidator and being fully advised in the premises, the Court by this Order hereby:

(1) Determines that the loss claim settlement as recommended for allowance is a loss for which Wisconsin Surety Corporation is liable, and accordingly approves such recommendation and allows payment of such loss claim settlement in the amount recommended by the Liquidator.

[(2) Approves such recommendation and disallows such claim in its entirety.]

[(3) Disapproves and modifies such recommendation as set forth in the attached Determination on Report or Claim.]

Distribution to the claimant of the amount allowed shall be according to the priorities recommended by the Liquidator.

[Portions of the amount allowed are eligible for distribution to the claimant in a class or classes lower in priority than Class 3. It is anticipated at this time that there will be insufficient assets to make any distribution to claimants in classes lower in priority than Class 3 and therefore that the above claimant will receive no distribution whatsoever regarding any portions eligible for distribution in Classes 4, 5, 6, 7, 8, 9, 10 and 11 inclusive, and that such claimant will receive no further notice regarding such portions.]

Dated: March 17th, 1987

BY THE COURT:

/s/ _____
Circuit Court, Branch 4
Dane County, State of Wisconsin

ATTACHMENT – C.D. 425A, B & C
and 436A, B & C

The claimant seeks recovery of $3,973.80, plus interest, for unpaid tax-related moneys alleged to be due directly from the insolvent insurance company, Wisconsin Surety Corporation. This claim is comprised of $3,281.74 (Claim 425C) for withholding and Federal Insurance Contribution Act taxes due from Wisconsin Surety Corporation; and of $692.06 (Claim 436C) for withholding due from Wisconsin Surety Corporation.

The claimant also seeks recovery of $50,854.14, plus interest, for actions taken by Wisconsin Surety Corporation under the provision of certain surety bonds issued by the insurer. This claim is comprised of $7,318.27 (Claim 425A) against Wisconsin Surety Corporation as surety for LTL Electrical Contractors, Inc.; $12,548.57 (Claim 425B) against Wisconsin Surety Corporation as surety for E. C. Construction Co., Inc.; $13,196.89 (Claim 436A) against Wisconsin Surety Corporation as surety for V & L Construction Co., Inc.; and $17,790.41 (Claim 436B) against Wisconsin Surety Corporation as surety for Vankeirsbelk Construction Company.

Claims 425A, 425B, 425C and 436B were disallowed by the Liquidator on June 18, 1980. The disallowance was mailed to the claimant, and no objection having been filed within 60 days, the Court ordered the claims disallowed on September 9, 1980. Claim 436A was disallowed by the Liquidator on June 18, 1980. The determination was mailed to the claimant, and no objection having been filed within 60 days, the Court disallowed the claim on September 12, 1980. Claim 436C was allowed in full by the Court on February 29, 1980, but the check issued to the claimant by the Liquidator in full payment has never been cashed and is now void.

On May 29, 1984 the liquidation proceedings were terminated. On or about February 6, 1985 representatives of the Office of the Commissioner of Insurance for the State of Wisconsin were notified that the claimant was

considering bringing an action against the Commissioner in federal court, asserting priority under Title 31, U.S.C. § 3713, and also asserting liability to the claimant under Title 31, U.S.C. § 3713. On February 18, 1987 the proceedings were reopened.

The claimant and the Liquidator have reached a formal settlement, by which the Liquidator has agreed to pay the claimant a total of $28,102.33, in return for a full release, in compromise of these disputed claims.

Accordingly, Claims 425A, 425B, 436A and 436B are allowed as class 3 claims, with the total amount for the four claims to be paid being $24,128.53; and Claims 425C and 436C are allowed in full as class 5 claims, with the aggregate amount to be paid being $3,973.80; for a total settlement to be paid forthwith to the claimant in the amount of $28,102.33.

Q:425.436

APPENDIX 2

Allied Fidelity
Insurance Co.

IN LIQUIDATION

TO: ALL STATE INSURANCE COMMISSIONERS, SUPERINTENDENTS AND DEPARTMENTS, ALL ANCILLARY RECEIVERS, AND ALL STATE INSURANCE GUARANTY FUNDS OR ASSOCIATIONS

FROM: INDIANA INSURANCE COMMISSIONER HARRY E. EAKIN, AS LIQUIDATOR OF ALLIED FIDELITY INSURANCE CO. ("AFIC")

DATE: JANUARY 13, 1988

RE: ALLEGED FEDERAL PRIORITY

Last September, the AFIC Liquidator sent to you an accounting, a duplicate copy of which is enclosed, which mentioned the uncertainty created by alleged federal priorities in the AFIC liquidation proceeding. See paragraphs 6 and 13 of the accounting. The uncertainty was heightened by the recent federal court decision in the Eastern Indemnity liquidation in Maryland. A copy of that decision is also enclosed.

While the AFIC Liquidator is still in the process of analyzing the thousands of claims received by the December 1 claim filing deadline, it looks as if the federal claims received will total in excess of $7 million. That being so, and until the AFIC Liquidator has had a chance to compile sufficient information to prepare a more complete report to the Court, each insurance department, ancillary receiver, and guaranty fund should make certain that no assets of AFIC

are used in a way that would arguably subject insurance departments, receivers or guaranty funds to the contention that the claimed federal priority has been violated. Obviously, departments, ancillary receivers or guaranty funds that are holding special deposits or other assets of AFIC need to be the most careful.